

ANNEX I

ANSWERS OF PARTIES TO THE PANEL'S QUESTIONS AND OTHER COMMENTS AND DOCUMENTS RECEIVED FROM PARTIES

Contents		Page
Annex I-1	Answers of Brazil to the Panel's Questions Posed Following the First Session of the First Substantive Meeting (11 August 2003)	I-3
Annex I-2	Answers of the United States to the Panel's Questions Posed Following the First Session of the First Substantive Meeting (11 August 2003)	I-77
Annex I-3	Comments of Brazil to Answers to Questions Posed by the Panel Following the First Substantive Meeting of the Panel (22 August 2003)	I-132
Annex I-4	Answer of the United States to the Additional Question from the Panel (27 August 2003)	I-169
Annex I-5	Answers of Brazil to the Panel's Questions Posed Following the Resumed Session of the First Substantive Meeting (27 October 2003)	I-170
Annex I-6	Answers of United States to the Panel's Questions Posed Following the Resumed Session of the First Substantive Meeting (27 October 2003)	I-235
Annex I-7	Answers of Brazil to the Panel's Questions Posed Following the Second Substantive Meeting (22 December 2003)	I-275
Annex I-8	Answers of United States to the Panel's Questions Posed Following the Second Substantive Meeting (22 December 2003)	I-344
Annex I-9	Comments of the United States of America Concerning Brazil's Econometric Model (22 December 2003)	I-396
Annex I-10	Answers of Brazil to the Panel's Additional Questions Posed on 23 December 2003 and 12 January 2004 (20 January 2004)	I-419
Annex I-11	Answers of United States of America to the Panel's Additional Questions Posed on 23 December 2003 (20 January 2004)	I-437
Annex I-12	Brazil's Comments on the 22 December US Comments Concerning Brazil's Econometric Model (20 January 2004)	I-440
Annex I-13	Brazil's Comments on the US Answers to Questions Posed by the Panel Following the Second Substantive Meeting of the Panel (28 January 2004)	I-467
Annex I-14	Comments of the United States of America on the Answers of Brazil to Further Questions from the Panel to the Parties following the Second Panel Meeting (28 January 2004)	I-552
Annex I-15	Brazil's Comments and Requests Regarding Data Provided by the United States on 18/19 December 2003 and the US Refusal to Provide Non-Scrambled Data on 20 January 2004 (28 January 2004)	I-612
Annex I-16	Comments of the United States of America on Comments by Brazil on US Comments Concerning Brazil's Econometric Model (28 January 2004)	I-648

Contents		Page
Annex I-17	Brazil's Answers to the Panel's Additional Questions Posed on 3 February (11 February 2004)	I-660
Annex I-18	Answers of the United States of America to the Panel's Additional Questions Posed on 3 February (11 February 2003)	I-664
Annex I-19	Comments of the United States of America on the Comments of Brazil to US Data Submitted on 18 and 19 December 2003 (11 February 2004)	I-677
Annex I-20	Brazil's Comments on US 11 February 2004 Answers to the Panel's Additional Questions (18 February 2004)	I-704
Annex I-21	Comments of the United States of America to the 11 February 2004, Answers of Brazil to Panel Question 276 (18 February 2004)	I-728
Annex I-22	Brazil's Comments on US 11 February Comments on Brazil's 28 January "Comments and Requests Regarding Data Provided by the United States on 18/19 December 2003 and the US Refusal to Provide Non-Scrambled Data on 20 January" (18 February 2004)	I-734
Annex I-23	Comments of the United States of America on the February 18, 2004, Comments of Brazil (3 March 2004)	I-796
Annex I-24	Responses of the United States of America to the Panel's February 3, 2004 Data Request, As Clarified on February 16, 2004 (3 March 2004)	I-819
Annex I-25	Answers of the United States of America to Question 264(b) Dated February 3, 2004, from the Panel to the Parties Following the Second Panel Meeting (3 March 2004)	I-825
Annex I-26	Brazil's Comments on US 3 March 2004 Data (10 March 2004)	I-827
Annex I-27	Brazil's Comment on US 3 March 2004 Answer to Question 264(b) (10 March 2004)	I-843
Annex I-28	Comments of the United States of America on the 10 March 2004, Comments of Brazil on the US Data Submitted on 3 March 2004 (15 March 2004)	I-845

ANNEX I-1

ANSWERS OF BRAZIL TO QUESTIONS POSED BY THE PANEL FOLLOWING THE FIRST SUBSTANTIVE MEETING OF THE PANEL

11 August 2003

TABLE OF CONTENTS

	<u>Page</u>
A. UPLAND COTTON	8
B. PRELIMINARY ISSUES	8
1. Product scope of Panel's terms of reference relating to Brazil's export credit guarantee claims	8
2. Expired measures	10
3. Agricultural Assistance Act of 2003.....	10
C. MEASURES AT ISSUE.....	12
D. ARTICLE 13(B): DOMESTIC SUPPORT MEASURES	14
1. "exempt from actions".....	14
2. "such measures" and Annex 2 of the Agreement on Agriculture	14
3. "do not grant support to a specific commodity"	21
4. "in excess of that decided during the 1992 marketing year"	29
E. EXPORT CREDIT GUARANTEE PROGRAMMES	47
F. STEP 2 PAYMENTS.....	68
G. ETI ACT	75

TABLE OF CASES CITED

Short Title	Full Case and Citation
<i>Brazil - Aircraft</i>	Appellate Body Report, <i>Brazil – Export Financing Programme for Aircraft</i> , WT/DS46/AB/R, adopted 20 August 1999
<i>Brazil – Aircraft (21.5)</i>	Panel Report, <i>Brazil – Export Financing Programme for Aircraft. Recourse by Canada to Article 21.5 of the DSU</i> , WT/DS46/RW, , adopted 4 August 2000
<i>Brazil – Aircraft (21.5)</i>	Appellate Body Report, <i>Brazil – Export Financing Programme for Aircraft. Recourse by Canada to Article 21.5 of the DSU</i> , WT/DS46/AB/RW, adopted 4 August 2000
<i>US – Shrimp (21.5)</i>	Panel Report, <i>United States – Import Prohibition of Certain Shrimp and Shrimp Products. Recourse to Article 21.5 by Malaysia</i> , WT/DS58/RW, adopted 21 November 2001
<i>Canada – Aircraft (21.5)</i>	Panel Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft, Recourse by Brazil to Article 21.5 of the DSU</i> , WT/DS70/RW, adopted 20 August 1999
<i>Canada - Aircraft</i>	Appellate Body Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft</i> , WT/DS70/AB/R, adopted 20 August 1999
<i>India – Patents (EC)</i>	Panel Report, <i>India – Patent Protection for Pharmaceutical and Agricultural Products</i> , WT/DS/79R, adopted 2 October 1998
<i>Canada – Dairy</i>	Appellate Body Report, <i>Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products</i> , WT/DS103/AB/R and WT/DS113/AB/R, adopted 27 October 1999.
<i>US - FSC</i>	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporation”</i> , WT/DS108/AB/R, adopted 20 March 2000.
<i>US – FSC (21.5)</i>	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporation” . Recourse to Article 21.5 of the DSU by the European Communities</i> , WT/DS108/AB/RW, adopted 29 January 2002.
<i>EC – Bed Linen (21.5)</i>	Appellate Body Report, <i>European Communities – Anti-Dumping Duties on Imports of Cotton – Type Bed Linen from India. Recourse to Article 21.5 of the DSU by India</i> , WT/DS141/AB/RW, adopted 24 April 2003
<i>Chile – Agricultural Products (Price Band)</i>	Appellate Body, <i>Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products</i> , WT/DS207/AB/R, adopted 23 October 2002.
<i>Canada – Aircraft II</i>	Panel Report, <i>Canada – Export Credits and Loan Guarantees for Regional Aircraft</i> , WT/DS222/R, adopted 19 February 2002.

LIST OF EXHIBITS

Agricultural Assistance Act of 2003, in P.L. 108-7	Exhibit Bra-135
P.L. 106-113	Exhibit Bra-136
P.L. 106-224	Exhibit Bra-137
P.L. 107-25	Exhibit Bra-138
68 Federal Register 20331, 20331-20332	Exhibit Bra-139
Pindyck, Robert S. and Rubinfeld, Daniel L., Microeconomics, 5 Edition (2002), Prentice hall, New Jersey.	Exhibit Bra-140
7 U.S.C. 5622	Exhibit Bra-141
Agricultural Outlook, USDA, May 2002	Exhibit Bra-142
Agricultural Statistics 2003, USDA	Exhibit Bra-143
G/AG/R/31	Exhibit Bra-144
US and State Farm Income Data, (United States and States 1997-2001), USDA	Exhibit Bra-145
Acreage, NASS, 28 June 2002	Exhibit Bra-146
Estimate of Support Granted by Commodity via Counter-Cyclical Payments. Agricultural Prices	Exhibit Bra-147
Statement of Administrative Action	Exhibit Bra-148
Agricultural Outlook, USDA, August 2002	Exhibit Bra-149
G/AG/N/USA/10	Exhibit Bra-150
“US Export Credit Guarantee Programs: What Every Importer Should Know About the GSM-102 and GSM-103 Programs”, USDA, November 1996.	Exhibit Bra-151
GAO, Statement of Allan I. Mendelowitz, Director, Trade, Energy and Finance Issues, National security and International Affairs Division, before the Task Force on Urgent Fiscal Issues of the Committee on Budget of the US House of Representatives, “Status Report on GAO’s Reviews of the Targeted Export Assistance Program, the Export Enhancement Program, and the GSM 102/103 Export Credit Guarantee Programs,” GAO/T-NSIAD-90-53, 28 June 1990.	Exhibit Bra-152

US Department of Agriculture Office of Inspector General Financial and IT Operations Audit Report of the Commodity Credit Corporation's Financial Statements for Fiscal Year 2000, Audit Report N° 06401-14-FM, June 2001	Exhibit Bra-153
US Department of Agriculture Office of Inspector General Great Plains Region Audit Report of the Commodity Credit Corporation's Financial Statements for Fiscal Year 2001, Audit Report N° 06401-4-KC, February 2002.	Exhibit Bra-154
US Department of Agriculture Foreign Agricultural Service, "Notice to GSM – 102 and GSM – 103 Programme Participants", 24 September 2002	Exhibit Bra-155
US Export-Import Bank, "Comparison of Major Features of Programs Offered by Ex-Im Bank and Commodity Credit Corporation for Support of Bulk Agricultural Commodities"	Exhibit Bra-156
US General Accounting Office, Report to the Chairman, Task Force on Urgent Fiscal Issues, Committee on the Budget, House of Representatives, "International Trade: Iraq's Participation in US Agricultural Export Programs", GAO/NSIAD-91-76, November 1990	Exhibit Bra-157
US Department of Agriculture, Office of Inspector General, Financial and IT Operations Audit Report, "Commodity Credit Corporation's Financial Statement for Fiscal Year 2002", Audit Report N° 06401-15-FM, December 2002	Exhibit Bra-158
US General Accounting Office, Report to Congressional Requesters, "Loan Guarantees: Export Credit Guarantees Programs' Costs are High", GAO/GGD-93-45, December 1992	Exhibit Bra-159
US Department of Agriculture, Office of the Chief Financial Officer, Credit, Travel, and Accounting Division, "Agriculture Financial Standards Manual (May 2003)	Exhibit Bra-160
US Federal Accounting Standards Advisory Board, Federal Financial Accounting and Auditing Technical Release 3, "Preparing and Auditing Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act", 31 July 1999.	Exhibit Bra-161
Government – Wide Audited Financial Statements Task Force on Credit Reform, "Issue Paper, Model Credit Programme Methods and Documentation for Estimating Subsidy Rates and the Model Information Store", 96-CR-7, 1 May 1996	Exhibit Bra-162
Office of Management and Budget Annual Training, Introduction to Federal Credit Budgeting, 24 June 2002	Exhibit Bra-163
US Department of Agriculture, Foreign Agricultural Service, "Revised FY 2001 and FY 2002 Annual Performance Plan".	Exhibit Bra-164

US Department of Agriculture, Foreign Agricultural Service, "Revised FY 2000 and FY 2001 Annual Performance Plan".	Exhibit Bra-165
US Department of Agriculture Foreign Agricultural Service, News Releases regarding extension of GSM 102 and GSM 103 guarantees to Dominican Republic, Morocco, Ghana, South Korea, Vietnam and Algeria	Exhibit Bra-166
12 Steps to Participating in the USDA Supplier Credit Guarantee Program, Step 5.	Exhibit Bra-167
US Department of Agriculture Foreign Agricultural Service, News Releases regarding extension of SCGP guarantees to Tunisia, Azerbaijan, Vietnam, South Korea, Japan and Nigeria	Exhibit Bra-168

A. UPLAND COTTON

1. **Please confirm that all information and data that you have provided to the Panel relating to "cotton" in fact relates to upland cotton only. BRA, USA**

Brazil's answer:

1. Brazil can confirm that, except as explicitly stated otherwise, all the data and references made by Brazil to "cotton" relate and will relate to "upland cotton" only.

B. PRELIMINARY ISSUES

Note to parties: As indicated in the cover note, the Panel has expressed its views in respect of the three United States requests for preliminary rulings. The Panel's questions reflected in this compilation relating to the requested preliminary rulings on which the Panel has expressed its views are those that were posed in the course of the first session of the first Panel meeting. This is to give an opportunity for the parties to transpose into writing their oral responses.

1. **Product scope of Panel's terms of reference relating to Brazil's export credit guarantee claims**
2. **Is Brazil's claim in relation to export credit guarantees against the measures said to constitute the GSM-102, GSM-103 and SCGP programmes in their entire application, or against the measures said to constitute the GSM-102, GSM-103 and SCGP programmes in their application to upland cotton, or both? BRA**

Brazil's answer:

2. Brazil confirms that its claims against GSM 102, GSM 103 and SCGP concern the programmes in their entirety and are *not* limited to their application to upland cotton.
3. **If the request for consultations in this dispute omitted certain products in relation to export credit guarantees, on what basis is it argued that it failed to identify the measures at issue in accordance with Article 4.4 of the DSU? USA**
4. **Is it argued that the export credit guarantee programmes concerning upland cotton are each a separate or independent measure, in that they operate independently? USA**
5. **Is there a specification in any legislation or regulation (or any other official government document) which limit or restrict the export credit guarantee programmes at issue exclusively to upland cotton? USA**
6. **For the purposes of the Panel's examination of Brazil's claims relating to GSM-102, GSM-103 and SCGP under the Agreement on Agriculture and the SCM Agreement, is accurate data and information available with respect to these export credit guarantee programmes concerning upland cotton alone (e.g. with respect to "long-term operating costs and losses")? In this respect, the Panel also directs the parties' attention to the specific questions below relating to the programmes. USA**
7. **Are commitments with respect to export subsidies under the Agreement on Agriculture commodity-specific? How, if at all, is this relevant? BRA, USA**

Brazil's answer:

3. Under Articles 3.3 and 8 of the Agreement on Agriculture, a Member can only grant export subsidies for agricultural products if that Member has an export subsidy reduction commitment for the agricultural product in question. The commodity specific aspect becomes relevant in Step 2 and ETI export subsidies because the United States scheduled no reduction commitments for upland cotton. In the case of the export credit guarantee programs challenged by Brazil, the commodity specific aspect becomes relevant only after the Panel has found that export credit guarantees are export subsidies within the meaning of the Agreement on Agriculture. At that stage, the Panel needs to examine whether (a) for the group of *unscheduled* commodities, which includes upland cotton, and (b) for each of *scheduled* commodities, there is a threat of circumvention of the US export subsidy reduction commitments. Brazil has set forth its arguments that GSM 102, GSM 103 and SCGP violate Article 10.1 of the Agreement on Agriculture for both scheduled and unscheduled commodities in paragraphs 295-305 of its First Submission.

4. The commodity-specific nature of export subsidy reduction commitments is, however, irrelevant for determining whether GSM 102, GSM 103 and SCGP in their application to all eligible products are within the Panel's terms of reference.

8. Does the United States confirm that the questions referred to by Brazil in paragraph 92 of Brazil's oral statement were posed to the United States in the consultations? USA

9. How does the United States respond to paragraph 94 of Brazil's oral statement? USA

10. What actual prejudice, if any, has the United States suffered as a result of the alleged omission of products other than upland cotton from the request for consultations? USA

11. Does the United States agree that Brazil's request for establishment of the Panel can be understood to indicate that Brazil's export credit guarantee claims relate to products other than upland cotton? How, if at all, is this relevant? USA

12. Please address issues and submit evidence regarding the three export credit guarantee programmes concerned relating to upland cotton and other eligible agricultural commodities in your answers to questions and rebuttal submissions. BRA, USA

Brazil's answer:

5. Brazil has presented its arguments and evidence concerning the three export credit guarantee programmes always with respect to all eligible agricultural commodities¹ and will continue to do so in its answers to these questions and in future submissions to the Panel.

13. Please include any argumentation and evidence to support your statement during the Panel meeting that the inclusion of such other eligible agricultural commodities would create additional "work" for the Panel with respect to each of these commodities under Article 13 of the Agreement on Agriculture. USA

¹ See paragraphs 252-314 of the First Submission of Brazil and paragraphs 116-133 of the Oral Statement of Brazil.

2. Expired measures

14. Please submit evidence regarding the programmes under the 1996 FAIR Act, in particular, production flexibility contract payments and market loss assistance payments, to the extent that they would be relevant to the Panel's determination under Article 13 of the Agreement on Agriculture in your answers to questions and rebuttal submission. USA

15. Do the parties agree that it is beyond a Panel's power to recommend a remedy for an expired measure? Could the Panel be required to examine "expired measures" in order to conduct its assessment of the matter before it? How, if at all, is Article 7.8 of the SCM Agreement relevant to these matters? BRA, USA

Brazil's answer:

6. The Panel must examine any continuing effects of subsidies provided by expired measures, and it can recommend a remedy for any such continuing effects. Brazil has set forth its arguments in that respect in paragraphs 4-7 of its Closing Statement at the First Substantive Meeting of the Panel with the Parties, as well as in paragraphs 141-144 of its Oral Statement at the same meeting. Subsidies provided under expired subsidy measures can be the source of present adverse effects. Preventing a panel from examining expired measures in its assessment of the matter before it would render the adverse effects provisions of the SCM Agreement a nullity, as a Member would be freed from any responsibility for the effects of its subsidies by, for example, simply letting the legislation expire and renewing it every year (or in even shorter periods). The Panel is, thus, required to analyze the effects of subsidies provided by production flexibility contract ("PFC") payments and market loss assistance payments in its assessment of Brazil's adverse effects claims. Disregarding those payments would not enable the Panel to conduct "an objective assessment of the matter before it", as it would disregard a source of present adverse effects.²

7. Article 7.8 of the SCM Agreement offers the Panel the possibility to recommend a remedy for the adverse effects from subsidies provided by expired measures. Under Article 7.8, a Panel can recommend that a Member withdraw the adverse effects of the expired measures. By virtue of DSU Appendix 2, Article 7.8, not DSU Article 19, provides the basis for remedies involving claims under Articles 5 and 6 of the SCM Agreement. In making recommendations under such claims, the Panel is not limited to a recommendation that a Member bring its measures into conformity with a covered agreement. Rather, a Panel finding adverse effects caused by a Member's actionable subsidies must recommend that the Member withdraw the subsidy or remove the adverse effects.

8. In sum, the Panel is required to objectively assess the present effects of PFC and market loss assistance payments on US production, US exports and prices of upland cotton. If it finds that these subsidies cause adverse effects within the meaning of Articles 5 and 6 of the SCM Agreement – as Brazil believes the Panel will find based on the arguments and evidence to be presented by Brazil on 9 September 2003 – the Panel should recommend that the United States remove the adverse effects pursuant to ASCM Article 7.8.

3. Agricultural Assistance Act of 2003

16. What, if any, prejudice in terms of the presentation of its case does the United States allege, should the Panel proceed to consider the measures constituting the cottonseed payments under the Agricultural Assistance Act of 2003? USA

² The analysis in this paragraph is relevant to the first paragraph of Brazil's Answer to Panel Question 19.

17. (a) What is the relationship of the Agricultural Assistance Act of 2003 to other legislation in the request for establishment of the Panel? BRA, USA

(b) Do the legal instruments follow directly one after another, or are there temporal gaps? Are payments authorized under a broad legislative authority or are they specific to each legal instrument? BRA, USA

(c) Please provide any implementing regulations. Do these implementing regulations resemble those relating to previous programmes or payments? Are payments made retrospectively? How if at all is this relevant? BRA, USA

Brazil's answer:

9. Cottonseed payments for MY 2002, as with the previous cottonseed payments in MY 1999 and 2000, were authorized by annual appropriations acts involving a variety of other legislative provisions that do not relate to cottonseed payments.³ Public Law 106-113, inter alia, appropriated funds otherwise unused for assistance to producers or first-handlers of the MY 1999 crop of cottonseed.⁴ The United States indicated in consultations that \$79 million had in fact been used for that purpose. Public Law 106-224, inter alia, appropriates \$100 million for assistance to producers and first-handlers of the MY 2000 crop of cottonseed.⁵ Public Law 107-25, inter alia, added an appropriation of \$84.7 million for assistance to producers and first-handlers of the same MY 2000 crop of cottonseed.⁶ No cottonseed payments were authorized for MY 2001. The Agricultural Assistance Act of 2003, inter alia, appropriated cottonseed payments for the 2002 crop in the amount of \$50 million.⁷

10. None of these statutory provisions contains any guidance on how USDA was to implement the cottonseed payments. Eligibility, administration, application and payment rates and details are all provided for in regulations. Brazil has provided in Exhibit Bra-32 the regulations applicable to the MY 2000 crop of cottonseed. Regulations governing payments for the MY 2002 crop of cottonseed were issued on 25 April 2003 and are set forth in Exhibit Bra-139. Comparing these regulations with the regulations that implement 2002 cottonseed payments⁸ demonstrates that both regulations are almost identical. In fact, the preamble to the 2002-crop regulations provides that “[p]revious 1999-crop and 2000-crop cottonseed programs were codified in 7 CFR part 1427. This rule follows the model set by those preceding programs.”⁹ Additionally the preamble to the regulations states:

Presumably, Congress expected the old programme to serve as the model for the new programme provided for in the new legislation as no dissatisfaction was expressed.¹⁰

11. This evidence demonstrates that the Cottonseed Payment Programme in MY 2002 was a continuation of the Cottonseed Payment Programme with respect to MY 1999 and 2000. The Agricultural Assistance Act of 2003 appropriated new funds for the MY 2002 crop to the existing programme (after no such appropriations took place for MY 2001). The 2002 cottonseed payments provided for in the Agricultural Assistance Act of 2003 are “future measures implementing”¹¹ the

³ Exhibit Bra-135 (Agricultural Assistance Act of 2003, in P.L. 108-7), Exhibit Bra-136 (P.L. 106-113), Exhibit Bra-137 (P.L. 106-224) and P.L. Exhibit Bra-138 (107-25).

⁴ Exhibit Bra-136 (Section 104 of P.L. 106-113).

⁵ Exhibit Bra-137 (Section 204(e) of P.L. 106-224).

⁶ Exhibit Bra-138 (Section 6 of P.L. 107-25).

⁷ Exhibit Bra-135 (Section 206 of P.L. 108-7).

⁸ Exhibit Bra-139 (68 Federal Register 20331).

⁹ Exhibit Bra-139 (68 Federal Register 20331, p. 20331).

¹⁰ Exhibit Bra-139 (68 Federal Register 20331, p. 20332).

¹¹ Brazil's Request For the Establishment of a Panel, WT/DS267/7, p. 2. See Appellate Body Report, *Chile – Agricultural Products (Price Band)*, WT/DS207/AB/R, paras. 135-136 and 144.

existing (but unfunded) Cottonseed Payment Program, which formed part of the request for consultations and which has been consulted upon. The MY 2002 cottonseed payments are therefore within the terms of reference of this Panel and Brazil is entitled to challenge the adverse effects caused by these payments.

12. Finally, the Agricultural Assistance Act of 2003 appropriated \$50 million in cottonseed payments expressly for the MY 2002 crop. Payments will be made after the United States has received all applications and has calculated the payment rate.¹² Since, payments are made after the 2002 crop has been harvested, payments can be considered to be made retrospectively. Yet, irrespectively of when the payments are made and irrespectively of the Panel's decision whether they form part of the Panel's terms of reference, they are made in respect of MY 2002¹³ and, therefore, these payments should be included in the calculation of the MY 2002 support to upland cotton for purposes of the test under Article 13(b)(ii) of the Agreement on Agriculture.

18. If the Panel is correct in understanding that cottonseed payments are divided between processors and producers, how is this reflected in Brazil's calculations? BRA

Brazil's answer:

13. Brazil has included the full amount of cottonseed payments in its peace clause calculations for MY 1999, 2000 and 2002 because cottonseed payments constitute support to upland cotton. This approach is consistent with the United States' notifications of these payments as product-specific support to upland cotton in its notification of domestic support for MY 1999.¹⁴

14. Brazil furthermore notes that the full amount of cottonseed payments is available to stimulate production and distort trade. Including the full amount of cottonseed payments is also consistent with basic principles of microeconomics that the incidence of a tax or subsidy does not depend on where in the processing chain the tax or subsidy is applied. The production or consumption effects of a tax or subsidy depends on supply and demand elasticities and market conditions, but these market impacts do not depend on whether government checks are written in the name of farmers or initial processors.¹⁵

C. MEASURES AT ISSUE

19. The Panel notes that Brazil's panel request refers, inter alia, to alleged "subsidies" and "domestic support" "provided" in various contexts. Please specify the measures, in particular, the legislative and regulatory provisions, by number and letter, in respect of which Brazil seeks relief and indicate where each is referred to in the panel request. BRA

Brazil's answer:

15. Brazil's Request for Establishment of a Panel ("Panel Request") challenges two types of domestic support "measures" provided to upland cotton and various different types of export subsidy measures. The first type of domestic support "measure" is the payment of subsidies for the production and use of upland cotton. These payments were and continue to be made between MY 1999 to the present (and will be made through MY 2007) through the various statutory and regulatory instruments listed on pages 2-3 of Brazil's Panel Request. Brazil referred to these payments at pages 2-3 of the Panel Request as "subsidies and domestic support provided under" or "mandated to

¹² Exhibit Bra-139 (7 CFR 1427.1107-1110 as provided in 68 Federal Register 20331, p. 20333).

¹³ See Brazil's answer to Question 34.

¹⁴ See Exhibit Bra-47 (G/AG/N/USA/43, p. 20).

¹⁵ Exhibit Bra-140 (Pindyck, Robert S. and Rubinfeld, Daniel L., *Microeconomics*, 5th edition (2002), Prentice Hall, New Jersey, p. 313-317).

be provided” under the various listed statutory and regulatory instruments. Brazil has tabulated the different types of payments (i.e., the measures) made under these legal instruments in paragraphs 146-149 of its First Submission. Brazil’s “Further Submission” on 9 September 2003 will provide considerable detail concerning the effects of the subsidies provided and mandated to be provided by the United States. It is these effects in respect of which Brazil seeks relief with respect to the first type of domestic support measures.

16. A second type of domestic support “measure” challenged by Brazil are legal instruments as such. The “legislative and regulatory provisions, by number and letter, in respect of which Brazil seeks relief” are those involving the 2002 FSRI Act and the 2000 Agricultural Risk Protection Act and in particular the following:¹⁶

- **Marketing loan/loan deficiency payments:** Sections 1201(a)-(b), 1202(a)(6), 1202(b)(6), 1204(b), 1205(a)(1), 1205(b), 1205(c)(1), 1608 of the 2002 FSRI Act and 7 U.S.C. 7286 (Section 166 of the 1996 FAIR Act as amended) and 7 CFR 1427.22 to the extent that these provisions require the provision of marketing loan and loan deficiency payments for all production of upland cotton.
- **Counter-cyclical payments:** Section 1104(a)-(f)(1) of the 2002 FSRI Act and 7 CFR 1412.503.
- **Direct payments:** Section 1103(a)-(d)(1) of the 2002 FSRI Act and 7 CFR 1412.502.
- **Step 2 Domestic Payments:** Section 1207(a) of the 2002 FRSI Act and 7 CFR 1427.103, 7 CFR 1427.104(a)(1), 7 CFR 1427.105(a), 7 CFR 1427.108(d) requiring cotton user marketing certificate (“Step 2”) payments to be made to domestic users of US upland cotton.
- **Crop Insurance payments:** Section 508(a)(8), 508(b)(1), 508(b)(2)(A)(ii), 508(b)(3), 508(e) and 508(k) of the 2000 ARP Act¹⁷ mandating the provision of crop insurance policies to farmers, premium subsidies to farmers and reinsurance to insurance providers to the extent that these provisions apply to upland cotton. Section 516 providing for unlimited funding of the crop insurance programme to the extent that these funds are available to upland cotton producers

17. Finally, Brazil challenges three types of export subsidies provided by the United States. Regarding Step 2 export subsidies, the measure Brazil challenges is Section 1207(a) of the FSRI Act, and 7 CFR 1427.103, 7 CFR 1427.104(a)(2), 7 CFR 1427.105(a), and 7 CFR 1427.108(d) requiring cotton user marketing certificate (“Step 2”) payments to be made to exporters of US upland cotton.¹⁸ Brazil also challenges as a “measure” subsidies provided by Step 2 export programme as actionable subsidies.

18. Regarding Brazil’s ETI Act claim, the measure challenged by Brazil is the FSC Repeal and Extraterritorial Exclusion Act of 2000, Public Law 106-519, 114 Stat. 2423 (2000), and in particular, Section 3 (entitled “Treatment of Extraterritorial Income”), which amends the US Internal Revenue

¹⁶ These Acts are referenced on page 2 of Brazil’s Panel Request (WT/DS267/7), and Brazil’s *per se* claim regarding these Acts and the regulations is referenced at page 4 of Brazil’s Panel Request.

¹⁷ Page 2 of Brazil’s Panel Request (WT/DS267/7) identifies the Agricultural Risk Protection Act of 2000.

¹⁸ Page 2 of Brazil’s Panel Request (WT/DS267/7) identifies the 2002 FSRI and the regulations in relation to Step 2 payments.

Code (IRC) by inserting into it a new Section 114, as well as a new Subpart E, which is in turn composed of new IRC Sections 941, 942 and 943.¹⁹

19. With respect to Brazil's export credit guarantee claims, the measures challenged by Brazil are the GSM 102, GSM 103 and SCGP programs as established and maintained by 7 U.S.C. 5622²⁰ and 7 CFR 1493.²¹ Brazil challenges 7 U.S.C. 5622(a)(1) and (b),²² which provide for the extension of export credit guarantees on terms better than those available on the marketplace. Furthermore, Brazil challenges the maintenance of the GSM 102, GSM 103 and SCGP programs at premium rates that are inadequate to cover the long-term operating costs and losses of the programs. Additionally, Brazil challenges the failure of 7 U.S.C. 5622 and 7 CFR 1493 to prevent circumvention (or the threat of circumvention) of the US export subsidy commitments under the Agreement on Agriculture. Brazil also challenges as a "measure" GSM 102, GSM 103 and SCGP export credit guarantees facilitating the production and export of US upland cotton as actionable subsidies and thereby causing adverse effects to the interests of Brazil.

D. ARTICLE 13(B): DOMESTIC SUPPORT MEASURES

1. "exempt from actions"

20. In paragraph 8 of its initial brief (dated 5 June, 2003), the United States argued that the word "actions" as used in the phrase "exempt from actions" in Article 13 of the Agreement on Agriculture includes the "bringing of a case" and consultations. In paragraph 36 of its first written submission (dated 11 July, 2003), the United States stated as follows:

"[P]rior to this point in the process, the DSU rules did not afford the United States any opportunity to prevent the dispute from proceeding through consultations and panel establishment automatically, regardless of the US insistence that its measures conform to the Peace Clause."

Is it the United States' understanding that the drafters used the phrase "exempt from actions" knowing that under the DSU it would not be possible fully to exempt "actions", as the United States interprets that term? USA

21. In US - FSC and US - FSC (21.5) the Appellate Body made findings under the SCM Agreement relating to export subsidies in respect of agricultural products without making a finding in respect of Article 13 of the Agreement on Agriculture. How is this relevant to the United States' interpretation of the phrase "exempt from actions" as used in Article 13? USA

2. "such measures" and Annex 2 of the Agreement on Agriculture

22. Please explain the difference, if any, between the meaning of "defined" and the meaning of "fixed" in the phrase "a defined and fixed base period" in paragraph 6(a) of Annex 2 of the Agreement on Agriculture. BRA, USA

¹⁹ Page 2 of Brazil's Panel Request (WT/DS267/7) identifies the ETI Act.

²⁰ Exhibit Bra-141 (7 U.S.C. 5622) codifies the relevant provisions of the 1978 Agricultural Trade Act as amended, identified on page 2 of Brazil's Panel Request (WT/DS267/7).

²¹ See Exhibit Bra-38 (7 CFR 1493). Pages 2 and 5 of Brazil's Panel Request (WT/DS267/7) identifies GSM 102, GSM 103, and SCGP programs.

²² Exhibit Bra-141 (7 U.S.C. 5622) codifies the relevant provisions of the 1978 Agricultural Trade Act as amended, identified on page 2 of Brazil's Panel Request (WT/DS267/7).

Brazil's answer:

20. The meaning of the term "defined" in relation to "base period" is the period of time used to define the parameters ("indicate the extent"²³) of the base period. The word "period" is defined as "a course or extent of time".²⁴ For example, the "defined" "base period" to determine the amount of upland cotton base acreage for the PFC (and market loss assistance) payments was the average planted and considered planted acreage during MY 1993-95.²⁵ The term "fixed" in relation to "base period" means that the "defined" base period cannot change or be updated. This is confirmed by the dictionary meaning of the term "fixed," which is "definitely and permanently placed or assigned; stationary or unchanging in relative position; definite, permanent, lasting."²⁶ In sum, a base period is first "defined" in terms of a period of time, and then that period remains definitely and permanently assigned.

23. Please explain the meaning of "a" in "a defined and fixed base period" in paragraph 6(a) of Annex 2 of the Agreement on Agriculture, the meaning of "the" in "the base period" in paragraphs 6(b), (c) and (d), and the difference between these and the phrase "based on the years 1986-88" in Annex 3. BRA, USA

Brazil's answer:

21. Paragraph 6(a) requires Members to establish clearly defined eligibility criteria for a de-coupled direct payment measure. These eligibility criteria must be taken from "a" defined and fixed base period of time. Paragraph 5 of Annex 2 makes it clear that all of the subparagraphs of paragraph 6 apply to the same type of de-coupled income support. Thus, a de-coupled income support measure with "a" "fixed base period" must also comply with Annex 2, paragraphs 6(b), (c) and (d). These subparagraphs use the phrase "after the base period." Because Article 6(a) establishes that there can only be "a" (single) "fixed" base period for a particular de-coupled domestic support measure, the use of the term "the" in 6(b)-(d) refers back to "a" "fixed" base period established in Article 6(a). Thus, a de-coupled income support measure can have only one "fixed" base period.

22. The Panel is faced with the question whether a Member can make minor adjustments to a decoupled support measure, label it a new decoupled support measure and then update the base period. Guidance for this question is provided by the first part of Annex 2, paragraph 6(a), which sets out a transparency requirement that eligibility criteria for decoupled support measures be determined by "clearly-defined criteria". In assessing whether one decoupled income support measure is essentially the same as a replacement decoupled income support measure, the Panel could examine the eligibility criteria for each set of measures. If the structure, design, and eligibility criteria have not significantly changed between the original measure (containing the "fixed base period") and its replacement, then there is no basis for any updating of the "fixed base period".

23. The factual question the Panel must address in this case is whether the "direct payment" programme in the 2002 FSRI Act contains similar design, structure, and eligibility criteria as the "production-flexibility contract payments" for upland cotton in the 1996 FAIR Act. The clearest evidence that the direct payment programme is the direct successor to production flexibility contracts is found in Section 1107(b) of the 2002 FSRI Act. It provides as follows:

If a producer receives all or any portion of the payment authorized for fiscal year 2002 under a production flexibility contract, the Secretary shall reduce the amount of

²³ The New Shorter Oxford English Dictionary, 1993 edition, p. 618 (definition of "define").

²⁴ The New Shorter Oxford English Dictionary, 1993 edition, p. 2163.

²⁵ See First Submission of Brazil, para. 46. See also Exhibit Bra-31 (7 CFR 1412.103) in connection with Exhibit US-3 (7 CFR 1413.7(c)).

²⁶ The New Shorter Oxford English Dictionary, 1993 edition, p. 962.

the direct payment otherwise due the producer for the 2002 crop year under section 1103 by the amount of fiscal year 2002 payment received by the producer under the production flexibility contract.²⁷

24. Trading PFC dollars for direct payment dollars makes perfect sense given the very close similarities in the eligibility criteria between PFC and direct payments reflected in the statutes and regulations governing each. This is best illustrated in the following table:

Similarities of Production Flexibility Contract and Direct Payments

Eligibility Criteria	Production Flexibility Contracts	Direct Payments
Payment contract	Annual fiscal payment based on 7 year contract ²⁸	Annual payment based on annual contract ²⁹
Eligible Recipients	“Producers” who assume all or part of the risk of producing a crop ³⁰	Same ³¹
Contract Acreage (Base Acreage)	MY 1993-95 ³²	MY 1993-95 or MY 1998-2001 ³³
Programme crops	7 Crops ³⁴	Same plus soybeans, other oilseeds, and peanuts ³⁵
Planting Flexibility and Restrictions	Limitations on fruits and vegetables (wild rice added in 2000). ³⁶	Same. ³⁷
Payment Yield	Base yield same as deficiency payment base average MY 1981-85 ³⁸	Same. ³⁹
Cotton Payment	Payment on 85% of base acres times base yield times 7.07 cents per pound ⁴⁰ on average between 1999-2001 for upland cotton ⁴¹	Payment on 85% of base acres times base yield times 6.67 cents per pound for upland cotton ⁴²
Compliance conditions	Abide by conservation compliance requirements ⁴³	Same. ⁴⁴

²⁷ Exhibit Bra-29 (Section 1107(b) of the 2002 FSRI Act).

²⁸ Exhibit Bra-31 (7 CFR 1412.101 and 1412.103)

²⁹ Exhibit Bra-35 (7 CFR 1412.401)

³⁰ Exhibit Bra-31 (7 CFR 1412.202)

³¹ Exhibit Bra-35 (7 CFR 1412.402)

³² Exhibit Bra-31 (7 CFR 1412.103)

³³ Exhibit Bra-35 (7 CFR 1412.201)

³⁴ Exhibit Bra-31 (7 CFR 1412)

³⁵ Exhibit Bra-35 (7 CFR 1412.103)

³⁶ Exhibit Bra-31 (7 CFR 1412.206)

³⁷ Exhibit Bra-35 (7 CFR 1412.407)

³⁸ Exhibit Bra-31 (7 CFR 1412.103)

³⁹ Exhibit Bra-35 (7 CFR 1412.301 and 1412.302)

⁴⁰ Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50). Brazil notes that these payment rates were not statutory rates but resulted from the allocation of a fixed amount of budgetary outlays to holders of upland cotton base under the PFC programme in MY 1999-2001.

⁴¹ Exhibit Bra-31 (7 CFR 1412.103)

⁴² Exhibit Bra-35 (7 CFR 1412.502(e))

⁴³ Exhibit Bra-31 (7 CFR 1410.20)

25. For an upland cotton producer with upland cotton base in MY 2001 and MY 2002, the direct payments available in MY 2002 were based on the following four elements: (1) yield (the average of the farm for MY 1981-85), (2) base acreage for the farm (resulting from either MY 1993-95 or MY 1998-2001 production), (3) only 85 percent of base acres could receive payment, and (4) the payment rate of \$0.0677 cents per pound (applied to base acreage x yield x .85). The production flexibility contract payment for that same upland cotton farmer in MY 2001 would have been based on (1) yield (the average for MY 1981-85), (2) base acreage resulting from MY 1993-95 production, (3) only 85 percent of base acres could receive payment, and (4) 5.99 cents per pound.⁴⁵ Thus, with the exception of the per pound payment rate – which increased under the 2002 FSRI Act – and the ability in 2002 to update base acreage, the payment formula was the same under both programmes.

26. In addition to these payment formula similarities, the eligibility criteria for an upland cotton producer in MY 2001 and MY 2002 are either identical or very similar under both programmes. For example, eligible recipients under both programmes are “producers,” defined in each programme as “an owner, operator, landlord, tenant, or sharecropper that shares in the risk of producing a crop”.⁴⁶ The “producer” under each programme could not plant fruits, vegetables, tree nuts or wild rice without either a forfeiture of all payments or a reduction of payments.⁴⁷ And each “producer” under both programmes had to maintain the land in agricultural use and adhere to conservation requirements.⁴⁸

27. In addition to the possibility to update the base acreage, another difference between the PFC and direct payment is the addition of three additional programme crops for purposes of the direct payment programme – soybeans, other oilseeds, and peanuts.⁴⁹ Further, instead of a single seven-year contract, annual contracts are entered into between USDA and “producers” who must demonstrate that they are eligible for payments based, *inter alia*, on demonstrating that they “share in the risk of producing a crop and are entitled to share in the crop available for marketing from the farm”.⁵⁰ The final difference was to set fixed amounts of payments per pound that did not decrease over the six-year term of the 2002 FSRI Act. The 1996 FAIR Act based the payment rate on annual budgeted amounts and as the budgeted amounts declined, the payment rate declined.

28. None of these changes to the direct payment programme in any way changed the eligibility criteria, the design, or the structure of the production flexibility programme as it applied to upland cotton producers. For the typical upland cotton producer farming on upland cotton base acreage, the only thing that changed was that the producer received the option to *increase* payments by updating base acreage and obtained an *increased* payment rate. Given the identical nature of most aspects of the production flexibility contract payments and direct payments, there was no basis to change the “fixed base period” of marketing years 1993-1995 for the calculation of these direct payments.

29. In light of this evidence, the Panel is not faced in this case with the situation where a Member significantly changes the structure, design, and eligibility criteria of an older measure. For example, if a Member replaces an amber box domestic support measure with a green box measure, the structure

⁴⁴ Exhibit Bra-35 (7 CFR 1412.203)

⁴⁵ Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50). Brazil notes that this payment rate was not a statutory rate but resulted from the allocation of a fixed amount of budgetary outlays to holders of upland cotton base under the PFC programme in MY 2001.

⁴⁶ Exhibit Bra-29 (7 CFR 1001(1) of the 2002 FSRI Act), Exhibit Bra-28 (Section 102(12) of the 1996 FAIR Act)

⁴⁷ Exhibit Bra-28 (Section 118 b(1) of the 1996 FAIR Act), Exhibit Bra-29 (Section 1106 b(3) of the 2002 FSRI Act).

⁴⁸ Exhibit Bra-31 (7 CFR 1410.20) and Exhibit Bra-35 (7 CFR 1412.203)

⁴⁹ Exhibit Bra-29 (Section 1101-1103 of the 2002 FSRI Act), Exhibit Bra-27 (“Side by Side Comparison of the 1996 and 2002 Farm Act, USDA).

⁵⁰ Exhibit Bra-29 (Section 1001(1) of the 2002 FSRI Act).

and eligibility criteria is likely to be sufficiently different to permit the establishment of a new “fixed” base period for the new measure. But replacing an older green box measure with a new alleged green box measure, which basically only updates the base period and thereby results in increased payments, violates the requirement of “a” “fixed” base period in Article 6(a).⁵¹

30. Finally, Brazil believes that Annex 3, paragraphs 9 and 11 provide contextual support for the requirement that “a” “fixed” base period for essentially the same measure should not be changed. For the purposes of calculating total AMS, Annex 3 establishes “a” “fixed” base period – 1986-1988 – for determining the reference price that serves as a basis for the formula approach to calculating AMS for price support measures. This base period could not be changed without eliminating the basis for calculating the total AMS and the required reductions in domestic support. Similarly, paragraphs 6(a) and 6(b) of Annex 2 require a fixed base period and prevent an updating of a base period for “green box” domestic support measures that remain essentially the same programme.

24. How often can a Member define and fix a base period in accordance with paragraph 6 of Annex 2 of the Agreement on Agriculture? BRA, USA

Brazil’s answer:

31. As set out in Brazil’s Answer to Panel Question 23, the answer is *never* if the replacement de-coupled direct payment measure has a comparable structure, design and eligibility criteria as the older de-coupled direct payment measure.

25. Does the United States consider that there is any ambiguity in the term “type of production” as used in paragraph 6(b) of Annex 2 of the Agreement on Agriculture? USA

26. Can the United States confirm Brazil’s assertions in paragraph 174 of its first written submission that the implementing regulations for direct payments prohibit or limit payments if base acreage is used for the production of certain crops? If so, can the United States clarify the statement in paragraph 56 of its first written submission that direct payments are made regardless of what is currently produced on those acres? Can the United States confirm the same point in relation to production flexibility contracts? USA

27. Does Brazil argue that any United States measure that does not comply with the fundamental requirement of paragraph 1 of Annex 2 of the Agreement on Agriculture is actionable independently of any failure of that measure to comply with the basic or policy-specific criteria in Annex 2? BRA

Brazil’s Answer:

32. Yes. A domestic support measure that does not meet the “fundamental requirement” of the first sentence of Annex 2, paragraph 1, cannot be considered to be properly in the “green box”. In addition to the arguments at paragraphs 163-172 of Brazil’s First Submission, Brazil provides additional rationale for this argument below.

33. The use of the words “fundamental requirement” in the first sentence of paragraph 1, Annex 2, demonstrates that the obligation contained in the sentence is separate and distinct from the obligation to meet the basic and policy-specific requirements set forth in Annex 2. The ordinary meaning of those words, in that context and in light of the object and purpose of the Agreement in Agriculture, support this interpretation.

⁵¹ See First Submission of Brazil, paras. 177-181.

34. The ordinary meaning of “requirement” is “a thing required or needed, a want, a need; something called for or demanded; a conditions which must be complied with”.⁵² Interpreted in the context of paragraph 1, Annex 2, it means that having no, or at most minimal, trade-distorting effects or effects on production is a condition for a domestic support measure, which must be complied with, for exempting this domestic support measure from the reduction commitments.

35. The word “fundamental” qualifies the word “requirement”. The ordinary meaning of the term “fundamental” is “going to the root of the matter; serving as the base or foundation; essential or indispensable”.⁵³ The use of this adjective emphasizes and underscores that the requirement that a measure does not have trade-distorting effects or effects on production is *essential and indispensable* for a domestic support measure to be exempted from reduction commitments.

36. In sum, the ordinary meaning of a “fundamental requirement” is an “essential and indispensable condition that must be complied with”. It follows that the fundamental requirement in the first sentence of Annex 2, paragraph 1 must be read as a stand-alone obligation and that it is untenable to relegate the obligation in the first sentence of Annex 2, paragraph 1 to a policy objective role that merely informs the rest of the Annex. Instead, it is a condition of central importance that all domestic support measures must meet in order to be exempted from reduction commitments. Its importance is such that it serves as the premise on which the basic and policy-specific criteria are predicated.

37. The principle of effective interpretation (*l'effet utile*), recognized by panels and the Appellate Body, requires that a treaty be interpreted to give meaning and effect to all the terms of the treaty. The first sentence of Annex 2, paragraph 1 of the Agreement on Agriculture, which imposes an obligation in clear and unequivocal terms, has to be accorded full meaning. Nothing suggests that recognizing the fundamental requirement as a stand-alone obligation would undermine or render inutile the obligation to conform to the basic and policy-specific criteria. To interpret the fundamental requirement as a policy objective that merely informs the rest of Annex 2 would detract from the unambiguous obligation that domestic support measures have no, or at most minimal, trade-distorting effects or effects on production.

38. The obligation to meet the fundamental requirement set forth in Annex 2, paragraph 1 is the overriding principle that determines whether a measure can be exempt from reduction commitments. The purpose of the disciplines on domestic support in the Agreement on Agriculture, made effective in part through the reduction commitments, is to eliminate trade and production-distorting effects of domestic support measures or permit these measures to only have at most minimal trade or production-distorting effects. Where a measure does not create trade-distorting effects or effects on production, the rationale for limiting the use of that support measure disappears. Conversely, where a measure *does* have trade-distorting effects or effects on production, it must be subject to reduction commitments, regardless of whether it complies with certain other basic or policy-specific criteria. To exempt a measure because a Member alleges that it is classified as a green box measure, despite having trade-distorting effects or effects on production, would be to accept a circular reasoning and would undoubtedly undermine the disciplines on domestic support measures.

39. Brazil has set forth the evidence demonstrating that production flexibility contracts and direct payments have more than a minimal effect on production and thus are inconsistent with the fundamental requirement of the first sentence of Annex 2, paragraph 1.⁵⁴ These production effects are not surprising given the fact that both PFC and direct payments limit payments based on the *type* of

⁵² The New Shorter Oxford English Dictionary, 1993 edition, p. 2557.

⁵³ The New Shorter Oxford English Dictionary, 1993 edition, p. 1042.

⁵⁴ First Submission of Brazil, paras. 163-172; 183-191; First Oral Statement of Brazil, paras 50-54, 57-61; Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting of the Panel 22 July 2003, paras. 20-28).

production. Further, the updating of the base acreage for the direct payment programme (which one third of all eligible US farms took advantage of to increase their base acres eligible to receive direct payments), created further production enhancing effects today (as well as in the future) as detailed by Professor Sumner in paragraphs 20-29 of his Statement at the First Meeting of the Panel on 22 July 2003.⁵⁵

40. Brazil finally notes that it follows from the first sentence of Annex 2, paragraph 1 that any domestic support measures not complying with one of the basic or policy-specific criteria in Annex 2 is to be presumed to violate the fundamental requirement that it have no, or at most minimal, trade-distorting effects or effects on production. This conclusion holds regardless of the finding of the Panel on the character of the first sentence of Annex 2, paragraph 1 as a stand-alone obligation.⁵⁶

28. Please explain the meaning of the word "criteria" in Articles 6.1 and 7.1. What effect, if any, does the use of the word "Accordingly" in paragraph 1 of Annex 2 of the Agreement on Agriculture have on the meaning of the preceding sentence? BRA

Brazil's Answer:

41. Articles 6.1 and 7.1 reference "criteria" in general, without a specific mention of "basic criteria", or "policy-specific" criteria. To give meaning to the "fundamental requirement" of Annex 2, paragraph 1, the use of the word "criteria" must encompass all the rules, standards, or requirements established by Annex 2 as conditions for determining whether a domestic support measure can be exempted from reduction commitments. There is no basis, therefore, on which to exclude the fundamental requirement in Annex 2, paragraph 1 from the criteria that a domestic support measure must meet to be exempted from the reduction commitments.

42. Brazil further notes that, while Article 6.1 refers to "criteria set out in this Article", nowhere in the subsequent sub-paragraphs of Article 6 can the word "criteria" be found. This suggests that the term "criteria" as used in the Agreement on Agriculture cannot be interpreted in such a way as to limit its coverage to "basic criteria" or "policy-specific criteria" in Annex 2. The word "criterion" means "a principle, standard or test by which a thing is judged, assessed or identified".⁵⁷ It follows that the term "criteria" encompasses all standards and tests set up by the provisions in the Agreement on Agriculture and its Annexes to which Article 6.1 and 7.1 refer. These standards and tests include the fundamental requirement in the first sentence of Annex 2, paragraph 1.

43. The word "accordingly" does not (and cannot be read to) emasculate a "fundamental requirement". It introduces the related but distinct obligation to conform to the basic and policy-specific criteria. "Accordingly" is defined as "in accordance with the logical premise". It is also defined as "harmoniously, agreeably," or "in natural sequence,"⁵⁸ or "appropriate, fitting".⁵⁹ The word "accordingly" indicates that the "basic criteria" are derivative of the more fundamental obligation in the first sentence of that same paragraph. "Accordingly" simply explains that because it is a fundamental requirement that domestic support measures have no, or at most minimal, trade-distorting effects or effects on production, it is necessary that the measures also meet certain basic criteria. Thus, the "fundamental requirement" is a premise, and the "basic criteria" in the second sentence of Annex 2, paragraph 1 are in accordance – *i.e.*, not contrary – to that fundamental requirement. Because the first is a premise of the second, it is incorrect, indeed illogical, to say that the second sentence takes precedence, subsumes or subordinates the first more fundamental obligation.

⁵⁵ See Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting of the Panel).

⁵⁶ See First Oral Statement of Brazil, para. 21.

⁵⁷ The New Shorter Oxford English Dictionary, 1993 edition, p. 551.

⁵⁸ The New Shorter Oxford English Dictionary, 1993 edition, p. 15.

⁵⁹ The New Shorter Oxford English Dictionary, 1993 edition, p. 15.

29. Please explain the meaning of the words "the fundamental requirement" as used in paragraph 1 of Annex 2 of the Agreement on Agriculture. USA

30. Do the parties consider that direct payments and production flexibility contract payments meet or met the basic criteria referred to in paragraph 1 of Annex 2 of the Agreement on Agriculture? BRA, USA

Brazil's Answer:

44. The direct payments and production flexibility contract payments meet the first basic criteria in paragraph 1(a) of Annex 2. With respect to the second basic criteria, Brazil is not alleging that either of these two types of payments "have the effect of providing price support to producers".

31. If the first sentence of paragraph 1 of Annex 2 is not a stand-alone obligation, then must new, non- or minimally trade-distorting measures that do not conform to the criteria listed in Annex 2 be classified as non-Green Box? BRA, USA

Brazil's Answer:

45. Yes. As explained in answer to Question 27 above, any domestic support measures that do not comply with the basic or policy-specific criteria in Annex 2 shall be presumed to violate the fundamental requirement in the first sentence of paragraph 1 of Annex 2 and must, therefore, be considered non green-box domestic support measures. This is true regardless whether the Panel concludes that the first sentence of paragraph 1 of Annex 2 is a stand-alone obligation.

32. If the first sentence of paragraph 1 of Annex 2 expresses a general principle which informs the interpretation of the criteria in Annex 2, please explain how this affects the assessment of the direct payments programme's compliance with paragraph 6 of Annex 2. USA

3. "do not grant support to a specific commodity"

33. According to the United States' interpretation of the word "grant", when can a Member claim that a measure is not exempt from action under Article 13(b)? What if the measure is enacted annually? Can the Member obtain a remedy in respect of that measure under the DSU? USA

(34) Does Brazil interpret the word "grant" as used in Article 13(b)(ii) of the Agreement on Agriculture to mean payment made in a specific year or payment made in respect of a specific year? BRA

Brazil's Answer:

46. Brazil interprets the word "grant" to mean "payment made in respect of a specific year".⁶⁰

35. Does a failure by a Member to comply in a given year with either the chapeau of Article 13(b) or the proviso in subparagraph (ii) of Article 13(b) impact its entitlement to benefit in an earlier or a later year from the exemption from action provided by Article 13(b)? BRA, USA

⁶⁰ See First Oral Statement of Brazil, para. 31 ("Thus, the neutral term 'decision' must be read consistently with 'grant.' In sum, a harmonious interpretation of 'decided' exists where the 'decision' is to fund marketing year 1992 non-'green-box' expenditures for a specific commodity.").

Brazil's Answer:

47. Yes. A failure of a Member's measures to meet in any given year the conditions of the peace clause lifts the entitlement to peace clause protection for the whole implementation period for all measures found to fail meeting the conditions of the peace clause. This conclusion applies to domestic support measures as well as export subsidies.

48. At the outset, Brazil would like to recall that the peace clause provides Members only limited protection from actionable and prohibited subsidy claims under the SCM Agreement and GATT Article XVI. Domestic support measures are only exempt from action under Articles 5 and 6 of the SCM Agreement and under GATT Article XVI:1, if the domestic support measures do not violate the Total AMS reduction commitments of a Member and if they do not grant support to a specific commodity in excess of that decided during the 1992 marketing year. Export subsidies are only exempt from actions under Articles 3, 5 and 6 of the SCM Agreement and GATT Article XVI, if they conform fully to the provisions of Part V of the Agreement on Agriculture.

49. The peace clause does not impose any positive obligations and can, thus, not be violated. It constitutes a right and defence of a Member that this Member may or may invoke. The *US – FSC* and *US – FSC (21.5)* dispute are examples of disputes, in which a Member has chosen not to invoke the peace clause defence. Brazil has demonstrated before, that the peace clause is in the nature of an affirmative defence.⁶¹ Accordingly, a complaining party does not bear the burden of proof that the measures at issue do not meet the conditions of the peace clause.

50. Nothing in the text of Article 13 suggests that a Member, which foregoes its peace clause exemption for particular measures in one year during the implementations period, shall be entitled to claim peace clause exemption for those measures for other – earlier or later – years. Article 13 offers peace clause exemption for measures that “fully conform” to Article 6 and that do not “grant support” “in excess of” that decided during the 1992 marketing year, as well as for measures that “fully conform” to Part V of the Agreement on Agriculture. If measures fail to meet one of the relevant conditions in any year – be it the current year or an earlier year during the implementation period – those measures can no longer be considered to “fully conform” or to not “grant support” “in excess of”. Consequently, those measures are not exempt from action.

51. Finally, Brazil notes that the Panel need not decide this issue due to the circumstances of the present case. Brazil has demonstrated that the United States' domestic support measures at issue in this dispute do not meet the conditions of the peace clause in any marketing year from MY 1999 to the present and that the US export subsidies also do not conform fully to Part V of the Agreement on Agriculture. Thus, none of the subsidies at issue in this dispute is entitled to exemption from actions pursuant to the peace clause.

36. Does a failure by a Member to comply with Article 13(b) in respect of a specific commodity impact its entitlement to benefit in respect of other agricultural products from the exemption from action provided by Article 13(b)? BRA, USA

Brazil's Answer:

52. No. In fact, this is one of the purposes of the word “specific” in Article 13(b)(ii) – to differentiate a specific commodity whose amount of support was greater than the amount of support in marketing year 1992 from other specific commodities whose support may not have exceeded the 1992 marketing year level.

⁶¹ See First Submission of Brazil, para. 110-121, and First Oral Statement of Brazil, para. 5-11.

37. In the United States' view, why did the drafters not use the exact term "product-specific" in Article 13(b)(ii)? USA

38. Given the fact that subsidies available for more than one product could have various effects on production, how does the United States demarcate between product-specific support and non-product specific support ? USA

39. If "such measures" in Article 13(b)(ii) refers to all those in the chapeau of Article 13(b), why are they not all included in the potential comparisons with 1992? In what circumstances can measures which grant non-product specific support lose exemption from action under Articles 5 and 6 of the SCM Agreement and Article XVI of GATT 1994? USA

40. In relation to which other provisions in the Agreement on Agriculture is it relevant to disaggregate non-product specific support in terms of specific commodities? BRA

Brazil's Answer:

53. The Panel's question uses the phrase "non-product specific support", which is not defined explicitly in the Agreement on Agriculture. Therefore, before responding to this question, Brazil will set forth its understanding of what this term means and which measures at issue in this dispute fall within that definition.

54. "Aggregate Measurement of Support" and "AMS" are defined in Article 1(a) as the "annual level of support, expressed in monetary terms" (a) "in favour of the producers of the basic agricultural product" or (b) "non-product-specific support provided in favour of agricultural producers in general . . ." (emphasis added). Brazil notes that the ordinary meaning of the word "general" is "including, involving, or affecting all or nearly all the parts of a (specified or implied) whole."⁶² The "whole" in the case of Article 1(a) of the Agriculture Agreement refers to agricultural producers of all or nearly all basic agricultural products covered by the Agreement on Agriculture. Because the universe of domestic support measures includes either "product-specific" or "non-product-specific" domestic support measures, it follows that any domestic support that is not provided "in favour of agricultural producers in general" is deemed to be "in favour of the producers of the basic agricultural product". Accordingly, the test for determining whether a domestic support measure is "non-product specific" for the purpose of calculating AMS is whether, as a factual matter, the measure provides support to "agricultural producers in general".

55. The United States has argued that Article 1(a) is useful context for interpreting the meaning of "support to a specific commodity".⁶³ However, the United States latches on to only the first part of Article 1(a), and ignores the "in general" qualification in the second part, which provides the essential meaning as to the scope of what is and is not "product-specific". Brazil notes that none of the measures it used to calculate the levels of support for purposes of Article 13(b)(ii) for MY 1992 or MY 1999-2002 could properly be deemed to be "non-product-specific" support as defined in Article 1(a) of the Agreement on Agriculture. And, as Brazil has previously argued, all of these measures are "support to" upland cotton within the meaning of Article 13(b)(ii).

56. With that introduction, the answer to the Panel's question is that Brazil is not aware of any provision of the Agreement on Agriculture requiring the dis-aggregation of support that is "provided in favour of agricultural producers in general", as discussed above. However, Brazil notes that Article 13(b)(ii) is a sui generis provision of the Agreement on Agriculture that does not use the phrases "AMS", "non-product specific" or "product-specific" support. Contrary to all of the other

⁶² The New Shorter Oxford English Dictionary, 1993 edition, p. 1073.

⁶³ First Submission of the United States, para. 78; See also Closing Statement of the United States, para. 18 (ignoring "in general" language).

provisions of the Agreement on Agriculture, Article 13(b)(ii) alone addresses the process for disciplining domestic support provided to a specific commodity under Articles 5 and 6 of the SCM Agreement and Article XVI:1 of GATT 1994.

41. What is the position of Brazil with regard to certain other domestic support measures not cited by Brazil that were notified by the United States as non-product-specific (e.g. G/AG/N/USA/43), some of which presumably deliver support to upland cotton (e.g. state credit programmes, irrigation subsidies etc). Why have budgetary outlays for such measures related to upland cotton not been included in the comparison of support with 1992? BRA

Brazil's Answer:

57. Brazil did not include any other types of domestic support measures for MY 1992 or MY 1999-2002 in calculating peace clause amounts because no other measures appeared to meet the test of being non-green box "support to" upland cotton in Article 13(b)(ii). Similarly, these measures appear to meet the test of being provided "in favour of agricultural producers in general". None of these other measures notified by the United States as non-product specific had any upland cotton specific link in terms of historic, updated, or present upland cotton acreage, present upland cotton production or prices, or upland cotton groups of insurance policies or any other specific upland cotton provisions. Further, the United States has not indicated in any documents that these state credit programmes, irrigation subsidies, etc. were not made available "in favour of agricultural producers in general". If the United States is able to provide such information, then it would be appropriate for the Panel to allocate such support to, inter alia, upland cotton. As detailed in Brazil's answer to Question 40, the United States was obligated to notify to the Committee on Agriculture and to allocate as "product-specific support" to upland cotton any domestic measure that did not provide support "in favour of agricultural producers in general. . .".

58. The only US domestic support measures that Brazil is aware of that would meet the test of being "support to upland cotton" are those that it listed for purposes of calculating the level of peace clause support in its First Written Submission.⁶⁴ In the view of Brazil, these non-green box domestic support measures are the measures that constitute "support to" upland cotton for the purpose of Article 13(b).

42. If the word "specific" were deleted from Article 13(b)(ii), would this change the meaning of the subparagraph? BRA

Brazil's Answer:

59. Brazil believes that the meaning would change. The deletion of the word "specific" would create some ambiguity. The ordinary meaning of the phrase "a commodity" is "a thing that is an object of trade, esp. a raw material or agricultural crop". Therefore, the meaning of a commodity is rather broad and could for instance refer to "grains".⁶⁵ While the term "grains" may refer to "a commodity," it cannot connote "a specific commodity". Specific commodities that make up the commodity "grains" would be wheat, barley, oats, rice etc. Thus, the use of the term "specific commodity" clarifies that the subject of Article 13(b)(ii) is support to specific, i.e., individual, commodities and that this provisions does not deal with groups of individual commodities such as grains.

⁶⁴ First Submission of Brazil, paras. 144, 148, 149.

⁶⁵ Also Annex 1 of the Agreement on Agriculture refers to some broad commodity categories such as "animal hair" and "essential oils." These would cover several specific commodities such as specific types of animal hair, or specific essential oils like jasmin oil or peppermint oil.

60. Further, the phrase “a specific commodity” also makes it clearer that the “commodity” at issue is equivalent to the “like product” as defined, *inter alia*, in the SCM Agreement. This parallel construction of the term “specific commodity” and “like product” is consistent with the fact that the peace clause provides a conditional exemption from Articles 5 and 6 of the SCM Agreement and Article XVI:1 of GATT 1994 – which require the examination of effects of subsidies on products “like” those receiving the subsidies.

43. What are the precise differences between deficiency payments and counter-cyclical payments that lead you to classify the former as product-specific and the latter as non-product specific? How do you classify market loss assistance payments? USA

44. Do you allege that counter-cyclical payments could be considered product-specific? BRA

Brazil's Answer:

61. Brazil notes its discussion of “non-product specific” and “product-specific” support in its Answers to Questions 40-41. For the purpose of calculating AMS, counter-cyclical payments (CCP) are “product-specific” support for two main reasons: (i) they are not “support provided in favour of agricultural producers in general”, and (ii) they are directly linked to upland cotton-specific parameters (current prices and historical acreage and yield). Indeed, when the US 2002 FSRI Act was examined by the WTO Committee on Agriculture, the European Communities agreed with Brazil that CCP payments could not be considered “non-product-specific” support.⁶⁶ New Zealand has taken a similar view in its Third Party Submission in this dispute.⁶⁷

62. Brazil has provided extensive facts that upland cotton producers receive CCP payments as support to upland cotton and that such payments are support to upland cotton for the purposes of Article 13(b)(ii). These facts also support a finding that CCP payments are “product-specific” support. Further, Brazil notes the following facts demonstrating that counter-cyclical payments (and direct payments) are not provided “in favour of agricultural producers in general”, but are instead provided to only a fraction of US agricultural production:

- CCP payments are made to holders of upland cotton base acreage when US upland cotton prices fall below 65.73 cents per pound. Producers/holders of all other farm acreage in the United States do not receive CCP payments when US upland cotton prices received by US producers fall. In MY 2001, (non-updated) upland cotton base acreage represented 1.7 percent of total US farmland.⁶⁸
- CCP payments for upland cotton (and direct payments) are received by holders of upland cotton base acreage, i.e. for land that grew upland cotton between 1998-2001 or between

⁶⁶ Exhibit Bra-144 (G/AG/R/31, para. 30) (“Brazil would not accept [CCP] classification as ‘non-product-specific payment.’”); para 31 (“The EC also shared Brazil’s analysis on how the counter-cyclical payments should be classified and pointed to US insurance programmes as not being properly classified at present”).

⁶⁷ Third Party Submission of New Zealand, para. 2.24 (“Accordingly, New Zealand considers that the United States incorrectly categorizes CCP payments as non-product specific support.”).

⁶⁸ In MY 2001, total US farmland was 959.163 million acres (See Exhibit Bra-143 (Agricultural Statistics 2003, USDA, Table 9.6). Average US upland cotton base acreage for MY 1997-2001 was 16.3 million acres (See Exhibit Bra-142 (Agricultural Outlook, USDA, May 2002, Table 19). Brazil has requested the United States to provide information on updated base acreage for the CCP and direct payment programme in questions during consultations and in the Annex V proceedings. Brazil has not received that information and, therefore, uses 16.3 million acreage as a proxy for the direct payment base acreage noting that USDA reports that more than 99 percent of eligible acreage signed up for the CCP and direct payment programme (Exhibit Bra-44 (“Direct Payment and CCP Enrollment Report,” USDA, 19 June 2003).

1993-1995. USDA reported in 2001 that the 1997 census showed there were 31,500 upland cotton farms. Assuming no increase in the number of US upland cotton farms since 1997, this represents 1.46 percent of all farms in the United States.⁶⁹

- Upland cotton cash receipts as a percentage of total cash receipts from all agricultural commodities was 2.5 percent in MY 1999, 2.35 percent in MY 2000, and 3.05 percent in MY 2001.⁷⁰
- The 10 “programme” crops in the CCP (and direct payment) programme represented only 23.49 per cent of total farm cash receipts from all agricultural commodities on average between MY 1997-2001.⁷¹
- The base acreage of the 10 “programme” crops in the CCP (and direct payment) programme represented only 30 percent of total US farm acreage in MY 2001.⁷²
- In MY 2002, CCP payments to holders of upland cotton base acreage represented approximately 80 percent – or \$1.143 billion – of total CCP payments (\$1.420 billion) for the ten eligible programme crops.⁷³
- In MY 2002, no CCP payments were made to holders of 8 of the 10 eligible crops. In particular, holders of base acreage for barley, corn, grain sorghum, oats, soybeans, other oilseeds, and wheat received no CCP payments.⁷⁴
- CCP base acreage receiving CCP payments in MY 2002 (upland cotton and rice base acreage) represented only 2.2 percent of total US farmland.⁷⁵
- 90 percent of US acreage eligible to receive upland cotton CCP payments for upland cotton is located in only 10 out of 50 US states, with the top 5 US States accounting for 66 percent of US upland cotton production.⁷⁶ Thus, upland cotton CCP payments are focused on farms in a limited number of US States (i.e., the “cotton belt”).

⁶⁹ Exhibit Bra-143 (Agricultural Statistics 2003, USDA, Table 9-9). There were 2.155 million farms in the United States in 2001. USDA reported that in 1997, there were 31,500 farms that grew cotton. Exhibit Bra-46 (“Cotton: Background and Issues for Farm Legislation,” USDA, July 2001, p. 2).

⁷⁰ Exhibit Bra-142 (Agricultural Outlook, USDA, May 2002, p. 59). The calculations cited above were derived from comparing upland cotton cash receipts compared to total commodity cash receipts net of government payments.

⁷¹ Exhibit Bra-145 (US and State Farm Income Data (United States and States 1997-2001), USDA, Table 5).

⁷² Brazil does not have access to actual CCP base acreage figures. Therefore, Brazil has used MY 2001 figures as a proxy and relies on MY 2001 PFC base acreage for the 7 crops covered by PFC payments (Exhibit Bra-142 (Agricultural Outlook, USDA, May 2002, p. 50) and has added MY 2001 soybean, peanut and other oilseed acreage (Exhibit Bra-146 (Acreage, NASS, 28 June 2002, p. 14, 15 and 17) (286.8 million acres). Total US farmland in 2001 was 959,163,331 million acres (Exhibit Bra-143 (Agricultural Statistics 2003, USDA, Table 9.6).

⁷³ Exhibit Bra-147 (“Estimate of Support Granted by Commodity via Counter-Cyclical Payments”).

⁷⁴ Exhibit Bra-147 (“Estimate of Support Granted by Commodity via Counter-Cyclical Payments”).

⁷⁵ Upland cotton and rice PFC base acreage represented 16.2 and 4.1 million acres (Exhibit Bra-142 (Agricultural Outlook, USDA, May 2002, p. 50)). Brazil does not have any information on the effects of the base acreage update and, therefore, uses the PFC base acreage as a proxy for CCP base acreage. Total US farmland in 2001 was 959,163,331 million acres (Exhibit Bra-143 (Agricultural Statistics 2003, USDA, Table 9.6).

⁷⁶ Exhibit Bra-107 (“US and State Farm Income Data, Farm Cash Receipts,” ERS, USDA, June 2003).

63. This evidence demonstrates that CCP (and direct payments) are provided to only a fraction of the producers of agricultural commodities in the United States and that payments are focused to producers of a limited number agricultural products. In view of these facts – particularly that upland cotton has its own “target price” of 72.4 cents per pound and accounted for 80 percent of all CCP payments in MY 2002 – it is appropriate for the Panel to consider only upland cotton statistics to conclude that these payments are “support to cotton” and are also “product-specific”.

64. But even if the Panel relies on data regarding all 10 CCP programme crops, the evidence still demonstrates that CCP and direct payments are “support to cotton” and “product-specific” support because they are not provided to producers of US agricultural commodities “in general”. Only around 30 percent of the farm acreage in the United States is farmed by producers with the possibility of receiving CCP payments.⁷⁷ In MY 2002, only 2.2 percent of total US farmland was eligible to receive CCP payments.⁷⁸ In light of these facts, it is not surprising that the EC correctly recognized in June 2002 that the US CCP programme does not represent a domestic support programme “provided in favour of agricultural producers in general”.⁷⁹

45. If the Panel considered that Step 2 payments paid to exporters were an export subsidy, would the United States count them as domestic support measures for the purposes of Article 13(b)? Please verify Brazil's separate data for Step 2 export payments and Step 2 domestic payments in Exhibit BRA-69 or provide separate data. BRA, USA

Brazil's Answer:

65. Brazil can verify that the Step 2 information its representatives received and that is tabulated in Exhibit Bra-69 was obtained from Wayne Bjorlie (wayne_bjorlie@wdc.usda.gov) in the Kansas City Commodity Office (KCCO) upon request for such data in December 2002.

46. What is the relevance, if any, of the concept of "specificity" in Article 2 of the SCM Agreement and references to "a product" or "subsidized product" in certain provisions of the SCM Agreement to the meaning of "support to a specific commodity" in Article 13(b)(ii) Agreement on Agriculture? BRA, USA

Brazil's Answer:

66. The concept of “specificity” in Article 2 of the SCM Agreement is useful context in interpreting the meaning of “support to a specific commodity” in Article 13(b)(ii). As the United States recognized at the First Meeting of the Panel with the parties, the word “support” as used in the Agreement on Agriculture is a synonym for “subsidy”.⁸⁰ The term “support to a specific commodity” has a similar meaning as “subsidized product,” as used in, inter alia, Article 6.3(c) of the

⁷⁷ Brazil does not have access to actual CCP base acreage figures. Therefore, Brazil has used MY 2001 figures as a proxy and relies on MY 2001 PFC base acreage for the 7 crops covered by PFC payments (Exhibit Bra-142 (Agricultural Outlook, USDA, May 2002, p. 50) and has added MY 2001 soybean, peanut and other oilseed acreage (Exhibit Bra-146 (Acreage, NASS, 28 June 2002, p. 14, 15 and 17) (286.8 million acres). Total US farmland in 2001 was 959,163,331 million acres (Exhibit Bra-143 (Agricultural Statistics 2003, USDA, Table 9.6).

⁷⁸ Upland cotton and rice PFC base acreage represented 16.2 and 4.1 million acres (Exhibit Bra-142 (Agricultural Outlook, USDA, May 2002, p. 50)). Brazil does not have any information on the effects of the base acreage update and, therefore, uses the PFC base acreage as a proxy for CCP base acreage. Total US farmland in 2001 was 959,163,331 million acres (Exhibit Bra-143 (Agricultural Statistics 2003, USDA, Table 9.6).

⁷⁹ Exhibit Bra-144 (G/AG/R/31, paras. 30-31).

⁸⁰ Brazil does not mean to imply that in the second phase of this proceeding it will not have the burden of demonstrating that each of the domestic support programs are “subsidies” within the meaning of the SCM Agreement.

SCM Agreement. Given the textual similarities between “subsidized product” and “support to a specific commodity”, assessment of whether “support to a specific product” exists could be examined with at least some reference to the specificity criteria of Article 2 of the SCM Agreement. Article 2 of the SCM Agreement provides, in relevant part:

- 2.1 In order to determine whether a subsidy, as defined in paragraph 1 of Article 1, is specific to an enterprise or industry or group of enterprises or industries (referred to in this Agreement as “certain enterprises”) within the jurisdiction of the granting authority, the following principles shall apply:
- (a) Where the granting authority, or the legislation pursuant to which the granting authority operates, explicitly limits access to a subsidy to certain enterprises, such subsidy shall be specific. . . .
 - (c) If, notwithstanding any appearances of non-specificity resulting from the application of the principles laid down in subparagraphs (a) and (b), there are reasons to believe that the subsidy may in fact be specific, other factors may be considered. Such factors are: use of the subsidy programme by a limited number of certain enterprises, predominant use by certain enterprises, the granting of disproportionately large amounts of subsidy to certain enterprises
- 2.2 A subsidy which is limited to certain enterprises within a designated geographical region within the jurisdiction of the granting authority shall be specific.

67. The US Statement of Administrative Action (“SAA”) describes in some detail how the United States intends to administer the specificity provisions, suggesting that the US Department of Commerce applies a low threshold for finding both “de jure” and “de facto” specificity:

The Administration intends to apply the specificity test in light of its original purpose, which is to function as an initial screening mechanism to winnow out only those foreign subsidies which truly are broadly available and widely used throughout an economy.⁸¹

Brazil agrees with this statement that the “original purpose” of the specificity criterion is to make subsidies non-specific only when they are broadly available and widely used throughout an economy.

68. The ordinary meaning of the plural term “certain enterprises,” as set out in the chapeau to ASCM Article 2.1, underscores that a subsidy can be specific even if it applies to a “group of . . . industries.” The term “industry” is defined as “a particular form or branch of productive labour; a trade, a manufacture”.⁸² Thus, the text of the chapeau supports the notion that for a subsidy to be specific under the SCM Agreement it must be limited to a certain number of industries that may be involved in different trades or manufacturing processes.

69. The object and purpose of the specificity requirement in Article 2.1(a) of the SCM Agreement is consistent with a broad scope for specificity. One key purpose for the specificity requirement is to avoid the countervailability of those subsidies widely available in an economy, while at the same time ensuring that those subsidies that benefit some groups of industries or enterprises more than others are covered. As the United States noted in the SAA:

The specificity test was intended to function as a rule of reason and to avoid the imposition of countervailing duties in situations where, because of the widespread

⁸¹ See Exhibit Bra-148 (“Statement of Administrative Action,” p. 929) (emphasis added).

⁸² The New Shorter Oxford English Dictionary, 1993 edition, p. 1356.

availability and use of a subsidy, the benefit of the subsidy is spread throughout an economy. Conversely, the specificity test was not intended to function as a loophole through which narrowly focused subsidies provided to or used by discrete segments of an economy could escape the purview of the CVD law.⁸³

70. Therefore, the ordinary meaning, context and object and purpose of Article 2.1(a) of the SCM Agreement confirm that subsidies that are available to discrete segments of an economy or to only particular industries are specific. Under these standards, each of the subsidies challenged by Brazil in this dispute (and listed as support for the purposes of the peace clause analysis) are provided to “discrete segments” of the US economy. Indeed, they are provided to discrete segments of the subsection of the US economy known as “agriculture”. Thus, if the Panel were to apply the specificity standard set out in Article 2 of the SCM Agreement to Article 13(b)(ii) of the Agreement on Agriculture, the identified domestic support subsidies would be considered “specific”.

71. Brazil notes that further support for the use of specificity concepts from the SCM Agreement in interpreting Article 13(b)(ii) of the Agriculture Agreement is found in the definition of “AMS” in Article 1(a) of the Agriculture Agreement. The definition of “non-product specific” support (“support provided in favour of agricultural producers in general”) illustrates that the concept of specificity in the context of the SCM Agreement and of AMS in the Agreement on Agriculture are similar. Both would require a finding of specificity unless support is provided to an economy generally, in the case of the SCM Agreement, or to “producers” of agricultural commodities “in general,” in the case of AMS under the Agriculture Agreement.

72. In contrast, the United States seeks to apply an extremely restricted concept of specificity to the peace clause that begins and ends with the question whether production of a specific commodity is required to receive the payment. This is one of the “policy-specific” criteria of a “green box” test in Annex 2, paragraph 6, but not the test of “support to a specific commodity” required by Article 13(b)(ii). Further, as demonstrated above, this narrow US interpretation finds no support in the provisions of the SCM Agreement and the Agreement on Agriculture that speak to specificity.

4. "in excess of that decided during the 1992 marketing year"

47. Where does Article 13(b)(ii) require a year-on-year comparison? BRA, USA

Brazil's Answer:

73. The text of Article 13(b)(ii) sets up a comparison between the “support” “grant[ed]” during the implementation period with support “decided” during the 1992 marketing year. Brazil cannot conceive of a methodology in which all support granted during the entire implementation period could be compared with the support decided during marketing year 1992. In order to generate an “apples to apples” (“support to support”) comparison, it is necessary to compare the support granted in any marketing year during the implementation period with the support decided during marketing year 1992. No other reading of Article 13(b)(ii) would permit the required comparison.

74. Additionally, Brazil notes that the second condition for domestic support measures to be exempted from actions under the SCM Agreement is that a Member’s domestic support measures conform fully to Article 6, and, thus, grant support within the limits of that Member’s Total AMS reduction commitments. These Total AMS reduction commitments are made on a yearly basis. The nature of the reduction commitment and the manner, in which compliance with Article 6 is determined, demonstrates that Article 13(b)(ii) – read in accordance with its chapeau and the reference to Article 6 therein – requires a year-by-year comparison. The context of the chapeau provides support for Brazil’s argument made above that the relevant comparison for Article 13(b)(ii)

⁸³ Exhibit Bra-148 (Statement of Administrative Action, p. 930).

involves a comparison of support granted in any of the marketing years during the implementation period with support decided in MY 1992.

75. Similarly, Article 13(c) provides further context to support the conclusion that Article 13(b)(ii) requires a year-by-year comparison. Brazil notes in its answer to Question 7, that export subsidy reduction commitments under the Agreement on Agriculture are made on a commodity-specific basis. Brazil has also pointed out in its answer to Question 79 that a violation of Part V of the Agreement on Agriculture, and the resulting loss of peace clause exemption, must also be assessed on a yearly basis.

48. Does Article 13(b)(ii) require a comparison of support granted with support decided? How could such a comparison be made? BRA, USA

Brazil's Answer:

76. The answer to the first question is yes, the text of Article 13(b)(ii) requires a comparison between the "support granted" for marketing years between 1995-2003 with the "support decided" in marketing year 1992. Brazil has explained in detail in its First Oral Statement the basis for this legal conclusion.⁸⁴

77. The second question asks how the comparison must be made. Brazil is of the view that a harmonious interpretation of "support decided" with "support granted" requires an examination of the expenditures incurred for all of the support related to the 1992 marketing year and each of the marketing years during the implementation period ending 1 January 2004. This expenditure approach permits an objective, easily verifiable approach to compare the support for each of the two time periods. That is particularly important when, as in this case, there are a wide variety of programmes that do not provide support on a "cents per pound" basis to all production. Brazil does not consider that a comparison based on a "rate of support" approach as suggested by the United States allows the same objective and easily verifiable comparison. Professor Sumner explained the difficulty of comparing, on a "cents per pound" basis, deficiency payments, Step 2, marketing loans, and crop insurance provided in marketing year 1992 with the marketing year 1999-2002 measures that replaced or changed the 1992 measures.⁸⁵ Nevertheless, Professor Sumner was able, through a relatively complex methodology, to calculate and compare a level of support on a per pound basis between marketing year 1992 and marketing years 1999-2002.

78. Another methodology is the rate of support taking into account expenditures, as detailed in Brazil's answer to Question 60 *infra*. Brazil would note that a last methodology that would have been possible, had the text of Article 13(b)(ii) included the term "AMS," would be to calculate support based on the criteria set forth in Annex 3 of the Agriculture Agreement. The results of this calculation are set forth in Brazil's answer to Question 67 *infra*.

49. Brazil claims that the terms "grant" and "decided" in Article 13(b)(ii) have broadly the same meaning. If so, why did the drafters not use the same term? BRA

⁸⁴ First Oral Statement of Brazil, para. 31.

⁸⁵ Exhibit Bra-105 (Statement of Professor Sumner at the First Meeting of the Panel).

Brazil's Answer:

79. Brazil set forth its interpretation of the terms “grant” and “decided” in its First Oral Statement.⁸⁶ Brazil concluded that the text, context, and object and purpose of Article 13(b)(ii) meant that the MY 1992 “decision” must be related to “support granted” in order to make possible the comparison between MY 1992 and marketing years during the implementation period. Yet, Brazil does not believe that the “decision” in marketing year 1992 means that all of the support had to be “granted” (i.e., paid) during the 12-month period of that single marketing year. Rather, the decision had to authorize payment in respect of a specific marketing year, including MY 1992.⁸⁷ However, a Member could have decided during the 1992 marketing year to budget a certain amount of support to specific commodities for the next several marketing years, including MY 1995 et seq. In that case, the relevant peace clause comparison would involve comparing the support granted to a specific commodity in any marketing year during the implementation period to what was decided during the 1992 marketing year to be provided for that later marketing year.

80. Brazil has cited the negotiating history of Article 13(b)(ii), which indicates that the EC insisted on the use of the word “decided” to obtain a safe harbour for the total quantity of its domestic support subsidies that it had already budgeted in marketing year 1992 for marketing year 1995 and thereafter.⁸⁸ Brazil will comment further, as required, on the intentions of the “drafters” following receipt of the answers of the European Communities and the United States.

50. Please provide any written drafting history which could shed light on why the proviso was added to what is now Article 13(b)(ii) and, in particular, why both words "grant" and "decided" were used. USA

51. Could the United States please comment on the interpretation advanced by the EC, in paragraphs 16 and 18 of its oral statement, of the words "decided during the 1992 marketing year"? USA

52. Please comment on an interpretation of the words "decided during" in Article 13(b)(ii) that would read them as synonymous with the words "authorized during". BRA, USA

Brazil's Answer:

81. Brazil agrees that in its proper context, the term “decided during” in Article 13(b)(ii) is synonymous with the words “authorized during”. Brazil has set forth the reasoning and citations supporting this conclusion in its Answers to Question 49 supra and Question 58 infra, as well as in its First Oral Statement at paragraph 31.

53. Assume, for arguments sake, that the only "decision" made in the United States in 1992 was the target price. How would Brazil make the comparison vis-à-vis, for example, the year 2001? BRA

Brazil's Answer:

82. Brazil maintains that the relevant comparison under Article 13(b)(ii) is to compare expenditures incurred relating to MY 1992 with expenditures incurred relating to marketing years during the implementation period. Only this methodology allows for a comparison irrespective of the nature and characteristics of the domestic support measures provided and does not suffer from the

⁸⁶ First Oral Statement of Brazil, paras. 27-34

⁸⁷ Brazil and the United States appear to agree that MY 1992 is the relevant marketing year for purposes of this dispute.

⁸⁸ First Submission of Brazil, para. 140.

shortcomings of other approaches, on which Brazil will comment below. In particular only an expenditure incurred approach allows for an effective comparison in the following situation: Assume, a Member introduces a payment that is made at a fixed rate per pound and is paid for each pound of actual upland cotton production. In this situation, it would be difficult to compare this domestic support measure, which is completely unrelated to market prices to a domestic support measure decided by a Member in MY 1992 and which sets a target price and provides price support.

83. With this qualification in mind, Brazil's understanding of this question is that the assumed single "decision" was the establishment of a target price of 72.9 cents per pound for eligible US upland cotton production during MY 1992. The assumed single "decision" on a target price of 72.9 cents per pound comprised of many other sub-decisions on the mandatory acreage reduction programme, on the operation of the 50/92-programme option, and on optional flex acres, among others.⁸⁹ Professor Sumner has analyzed in detail the process through which such a target price of support could be compared to the support provided in MY 1999-2002.⁹⁰ For MY 1992, he found that the estimated per unit support rates for all programs was 60.41 cents per pound. For MY 2001, he found the per unit support rates for all programmes was 66.51 cents per pound. Brazil refers to Professor Sumner's detailed description of the methodology he used to make these calculations.⁹¹

84. The irrationality of the simplistic "72.9 is greater than 51.92" approach by the United States is revealed by comparing it with the results of Professor Sumner taking into account in the calculation of the "rate of support" eligibility criteria and the costs imposed by participation in the US upland cotton support programs. It is also demonstrated by comparing the expenditures in MY 1992 (\$1.9 billion) with the expenditures in MY 2001 (\$4 billion).

54. Please identify all United States legal and regulatory and administrative instruments decided during the marketing year 1992, with the respective dates of decision, that decided support for upland cotton. BRA, USA

Brazil's Answer:

85. Brazil will comment further upon receipt of the answer provided by the United States to this question. The United States obviously has access to records related to all the decisions taken by the United States concerning its support programs for MY 1992. However, Brazil notes that given its understanding of the operation of the US support programmes, the United States took a number of decisions with respect to the upland cotton support programmes for MY 1992.

86. Many of the US support programmes for MY 1992 were decided by Title V of the Food, Agriculture, Conservation and Trade (FACT) Act of 1990 (P.L. 101-624), which established US farm policy for the 5 crop years 1991/92-1995/96, and by the Omnibus Budget Reconciliation Act (OBRA) of 1990 (P.L. 101-508), which established several programme provisions in order to reduce programme costs. Brazil considers that among the decisions taken by the United States in relation to MY 1992 upland cotton support programmes were the following:

- Continuation of the upland cotton target price under the deficiency payment programme at the 1990 level of 72.9 cents per pound set by the 1990 FACT Act. The OBRA limited the maximum payment acreage at 85 percent of the crop acreage minus the acreage reduction programme requirement, which was set annually. Therefore, the United States had to take a decision with respect to the MY 1992 percentage of deficiency programme

⁸⁹ For a more thorough discussion of the decisions Brazil understands the United States has taken with respect to MY 1992, see Brazil's answer to Question 54.

⁹⁰ See Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting of the Panel).

⁹¹ Annex 2 to Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting of the Panel).

base acreage that would be required to be set aside under the acreage reduction programme.

-
- In connection with the former, the United States also took a decision allowing producers to plant up to 25 percent of upland cotton acreage base, the so-called “flex acreage,” to any commodity except fruits and vegetables and mung beans.
- Furthermore, the United States had to decide on how to implement the 50/92-programme option under the deficiency payment program.
- The United States also needed to determine the upland cotton acreage base for purposes of the deficiency payment programme, which for MY 1992 represents the previous three-year average of planted and considered planted upland cotton acreage.
- Concerning the deficiency payment program, the United States finally had to decide on the payment rate for upland cotton.
- Concerning the marketing loan programme, the United States had to take a decision setting the marketing loan rate for upland cotton.
- Furthermore, the United States had to establish a weekly “adjusted world price” and, thus, the repayment rate for marketing loans determining the rate of marketing loan gains or loan deficiency payments.
- Furthermore, the United States took a weekly decision in MY 1992 with respect to the Step 2 payment rate applicable for that week.
- Regarding crop insurance, the Federal Crop Insurance Act of 1980 was the authorizing legislation, but it was necessary to adopt decisions concerning individual insurance policies that would apply to upland cotton and to set the respective rates of premium subsidies.

87. While Brazil does not consider this list to be exhaustive, it gives the Panel an overview on the variety of decisions the United States had to take to make the support programme to upland cotton operational. Brazil looks forward to the answer provided by the United States and reserves its right to comment as appropriate.

55. Please provide a copy of the instrument in which the rate of support for upland cotton during the marketing year 1992 was decided, indicating the date of the decision. USA

56. Could the United States please explain how support granted under legislation that dates back to 1990 can have been support "decided during the marketing year 1992"? USA

57. If the United States decided on a rate of support for MY1992, does that not mean that it decided on whatever budgetary outlay was required to meet that rate of support, even if the exact amount was not known at that time? USA

58. Please comment on the argument advanced by the EC, in paragraph 17 of its oral statement that: "Had WTO Members intended a limitation to the support provided or granted in 1992 the word 'for' would have been used in place of 'during'." BRA

Brazil's Answer:

88. Brazil agrees with the EC that the word “during” does not mean that all of the support need be provided or granted within the 12-month period of marketing year 1992. Rather, the decision must have been related to the amount of support to be granted in respect of marketing year 1992. This interpretation is consistent with an expenditure methodology that compares expenditures for upland cotton in respect of MY 1992 with expenditures for upland cotton in MY 1995-2003, and thereby permits a comparison of 1992 levels of support with levels of support in marketing years 1995-2003.

89. The negotiating history cited by Brazil in its First Submission indicates that the EC is in a special situation vis-à-vis the peace clause.⁹² It apparently made the decision in marketing year 1992 to budget an amount of support for commodities for marketing years 1995-2000 in its CAP reform. Brazil agrees with the EC that Article 13(b)(ii) was “intended to set up as a benchmark an amount of support adopted by some form of decision (be it political, legislative or administrative) in which support for a specific product is decided . . .” But the EC qualifies this assertion with the notion that that decision can only be “allocated for future years.”⁹³ This qualification would appear to be compelled by the EC’s particular situation. But that situation does not justify the EC’s conclusion that its “future years” concept means that Article 13(b)(ii) “clearly is not intended to set up a comparison between domestic support granted in 1992 and domestic support granted in a more recent period.”

90. The notion of a “decision” suggests that individual Members each made some sort of a decision with respect to the peace clause. The United States and Brazil agree that the decision made by the United States – whatever it may have been – related to the level of support provided to upland cotton in MY 1992. Brazil’s argument with the United States concerns the type of decision and the methodology that can be used to account for the level of support decided during MY 1992.

59. Should the rate of support as indicated in Article 13(b)(ii) include the market price? If so, why is it appropriate to include it in the comparison under Article 13(b)(ii)? BRA, USA

Brazil's Answer:

91. The most natural measure of support is budgetary expenditures, and these implicitly include market price in the sense that, for several US upland cotton programs, higher market prices lead to lower budgetary outlays. The US Government payments under the marketing loan, deficiency and counter-cyclical programs all decline with increasing market prices, as they cover the difference between the loan rate or the target price and the market price. Step 2 payments are also related to market prices in that they cover the difference between the A-Index and the lowest-priced US quote for upland cotton and, therefore, vary with market prices.⁹⁴ Incorporating the different degrees to which the market price influences the support provided by the US Government to its upland cotton farmers is best achieved by looking at the results in terms of budgetary outlays for the programs. This measure of support is straightforward to apply and allows a ready and accurate comparison between 1992 and subsequent marketing years.

92. Under the US approach and Professor Sumner’s adaptation of the US approach, market prices enter the calculation of the “rate of support” in the sense that the expected rate of support from the loan rate and the target price per eligible unit of production includes revenue expected to be received from the market (expected market price) and revenue expected from the US Government (subsidies). The market price enters inversely in the sense that the outlay is inversely related to the market price, as for instance the loan rate benefits make up the difference between the loan rate and the adjusted

⁹² First Submission of Brazil, para. 140.

⁹³ Oral Statement of the European Communities, 24 July, para. 18.

⁹⁴ Brazil notes, however, that the relationship between market price and level of Step 2 payments by the US Government is not as straightforward and positively correlated as for the other price-based programmes.

world price for the eligible share of production.⁹⁵ The higher the market price, the higher the resulting budgetary outlays.

93. Additionally, there is one further important reason why the notion of support in Article 13(b)(ii) should include the market price. Without reference to the market price, it is impossible to say what the rate of support means to farmers. It may be that the support is completely irrelevant, because market prices are much higher than the loan rate or the target prices set by the US Government. For instance, the loan rate was irrelevant for US upland cotton producers in MY 1994-1996,⁹⁶ because market prices were so high that no payments occurred. However, under essentially the same program, market loan benefits amounted to 26.6 cents per pound in MY 2001.⁹⁷ Thus, without taking market prices into account, it is impossible to translate a “rate of support” into actual support provided and to give meaning to the term “support.”

60. Can you provide information on support decided in 1992 and the years with which you believe it should be compared, on a per support programme / per unit of production / per annum basis? If possible, please specify how, if at all, budget outlays may be transposed into units of production, and which units of production are best to use. BRA, USA

Brazil's Answer:

94. Brazil maintains that the appropriate measure of support decided during MY 1992 is total actual expenditures resulting from any decisions regarding support to upland cotton. This must then be compared to total actual expenditures for support to upland cotton for MY 1999, 2000, 2001 and 2002. Presenting expenditures as a “rate of support” per pound of upland cotton disguises the fact that US expenditures for upland cotton have increased considerably since MY 1992. This is due to the fact that the increased US expenditures are now spread over an also increased US production. Therefore, a “rate of support” based on budgetary outlays or expenditure understates the real increase in US support to upland cotton. However, even disregarding the underestimation of the amount spent for upland cotton by presenting the budgetary outlays in the form of support per pound of actual upland cotton production, the data presented below show that also this measurement demonstrates that the US support in MY 1999-2002 is higher in each year than it was in MY 1992.

95. In answering this question, and responding to the Panel's requests, Brazil presents the support provided by the various US support programmes for a given marketing year on a per pound of actual upland cotton production basis. This approach takes into account market prices. Thus, the “support level” from deficiency payments, from the marketing loan programme and from counter-cyclical and Step 2 payments no longer reflects the “target price” approach favoured by the United States, but reflects actual payments made per unit of actual production.

96. Brazil believes that the unit of production that should be used is a pound of upland cotton actually produced in the United States for that marketing year in question. US support programmes provide support based on actual production (marketing loan programme, Step 2 and cottonseed payments), actual acres planted (crop insurance), updated historical production and current prices (deficiency payments and counter-cyclical payments), historical production (PFC, market loss assistance), and finally, updated historical production (direct payments). The most natural comparison on a per unit basis is to use actual production. The US National Cotton Council also calculates the support provided by all of these programmes to its upland cotton producer members in “cents per pound” of actual production.⁹⁸ This reflects the reality that an upland cotton farmer

⁹⁵ Brazil notes that budgetary outlays have not been part of Professor Sumner's calculation of the rate of support provided by the marketing loan, deficiency payment and CCP payment program.

⁹⁶ Exhibit Bra-4 (“Fact Sheet: Upland Cotton,” USDA, January 2003, p. 5-6).

⁹⁷ See Brazil's answer to question 60.

⁹⁸ Exhibit Bra-109; Exhibit Bra-111; Exhibit Bra-112.

seeking to remain in business must calculate whether the amount of government support plus market revenue compensates for the cost of production incurred by producing a pound of upland cotton.

97. Brazil arrives at the figures presented in the following table by dividing the total annual amount of budgetary outlays to upland cotton from a US support programme by the total amount of production of upland cotton in the relevant marketing year.

Support Per Pound Of Upland Cotton By Year And Support Programme

Year Programme	1992	1999	2000	2001	2002
	----- cents/pound -----				
Deficiency Payments ¹	13.49	none	none	none	none
PFC Payments ²	none	7.00	6.71	4.81	none
Market Loss Assistance Payments ³	none	6.97	7.15	6.65	none
Direct Payments ⁴	none	none	none	none	6.04
Counter-cyclical Payments ⁵	none	none	none	none	12.43
Marketing loan (Loan gains and LDP) ⁶	9.86	19.75	6.72	26.63	11.85
Step 2 Payment ⁷	2.74	5.39	2.93	2.09	3.95
Crop Insurance ⁸	0.35	2.17	2.00	2.79	2.42
Cottonseed Payment ⁹	none	1.01	2.29	none	0.62
Total	26.44	42.29	27.8	42.97	37.31

Notes

¹ Deficiency payment per pound of actual production = deficiency payment expenditure / (total production [bales] * 480 [pounds/per bale]). Total deficiency payments in MY 1992 were \$1.0174 billion, while total production was 15,71 million bales (Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 4-6)). One bale equals 480 pound of upland cotton.

² PFC payment per pound of actual production = PFC payment expenditure for upland cotton base * (actual upland cotton acreage / PFC upland cotton base acreage) / (total production [bales] * 480 [pounds/per bale]). Total PFC payments to upland cotton are taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 6). This amount has been adjusted by the ratio of upland cotton acres actually planted (Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4)) to upland cotton base acres in the PFC programme (Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)). This adjustment is necessary because only the portion of upland cotton PFC payments that actually benefits acres planted to upland cotton can be considered support to upland cotton. Because the latter figure is higher than the former, this leads to a reduction in the payment rate reflecting actual production in each year. Total production is taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4).

³ Market loss assistance payment per pound of actual production = Market loss assistance expenditure for upland cotton base * (actual upland cotton acreage / PFC upland cotton base acreage) / (total production [bales] * 480 [pounds/per bale]). Total market loss assistance payments to upland cotton are taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 6). This amount has been adjusted by the ratio of upland cotton acres actually planted (Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4)) to upland cotton base acres in the PFC programme (Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)). This adjustment is necessary because only the portion of upland cotton market loss assistance payments that actually benefits acres planted to upland cotton can be considered support to upland cotton. Because the latter figure is higher than the former, this leads to a reduction in the payment rate. Total production is taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 4).

⁴ Direct payments per pound actually produced = total direct payment expenditure for upland cotton base * (actual upland cotton acreage/direct payment upland cotton base acreage) / (total production [bales] * 480 [pounds/per bale]). Total direct payments for MY 2002 have been re-estimated from the figure presented by Brazil in its First Submission, para. 59. The new figure is based on the statutory payment rate of 6.67 cents per pound of upland cotton base multiplied by the direct payment upland cotton base acreage of 16.3 million acres (Brazil has assumed it to be the previous 5-year average as reported by USDA in Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)) multiplied by the direct payment yield of 604 pounds per acre (Brazil has assumed it to be the previous 5-year average as reported by USDA in Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)). Payments are made on 85 percent of base acres. This translates into a total of \$558.17 million. This amount has been adjusted by the ratio of upland cotton acres actually planted Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4) to upland cotton base acres in the direct payment program. Because the latter figure is higher than the former, this leads to a reduction in the direct payment rate. This adjustment is necessary because only the portion of upland cotton market loss assistance payments that actually benefits acres planted to upland cotton can be considered support to upland cotton. Total production is taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 4).

⁵ Counter-cyclical payments per pound actually produced = total counter-cyclical payment expenditure for upland cotton base * (actual upland cotton acreage / counter-cyclical payment upland cotton base acreage) / (total production [bales] * 480 [pounds/per bale]). Total counter-cyclical payments for MY 2002 have been re-estimated from the figure presented by Brazil in its First Submission, para. 69. The new figure is based on the MY 2002 payment rate of 13.73 cents per pound of upland cotton base multiplied by the counter-cyclical payment upland cotton base acreage of 16.3 million acres (Brazil has assumed it to be the previous 5-year average as reported by USDA in Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)) multiplied by the counter-cyclical payment yield of 604 pounds per acre (Brazil has assumed it to be the previous 5-year average as reported by USDA in Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)). Brazil notes that this underestimates the payments, as it disregards the yield update for purposes of the counter-cyclical payments). Payments are made on 85 percent of base acres. This translates into a total of \$1,148.98 million. This amount has been adjusted by the ratio of upland cotton acres actually planted Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4) to upland cotton base acres in the counter-cyclical payment programme. Because the latter figure is higher than the former, this leads to a reduction in the direct payment rate. This adjustment is necessary because only the portion of upland cotton market loss assistance payments that actually benefits acres planted to upland cotton can be considered support to upland cotton. Total production is taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 4).

⁶ Marketing loan benefit per pound of actual production = total marketing loan expenditures / (total production [bales] * 480 [pounds/per bale]). Total marketing loan payments (marketing loan gains plus loan deficiency payments) are taken para. 144, 148-149 of the First Submission of Brazil. Total production is taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 4).

⁷ Step 2 payments per pound of actual production = total Step 2 expenditures/(total production [bales] * 480 [pounds/per bale]). Total Step 2 payments are contained in Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 6). Brazil has estimated the MY 2002 amount at note 335 in its First Submission to be \$317 million. The amount of production has been taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 4). Brazil notes that the difference between 3.95 cents per pound resulting from this calculation and 4 cents per pound – which was the basis for Brazil to calculate the total Step 2 payment for MY 2002 – is due to rounding effects.

⁸ Crop insurance payments per pound of actual production = total crop insurance expenditures / (total production [bales] * 480 [pounds/per bale]). Total crop insurance payments are taken from Exhibit Bra-57 ("Crop Year Statistics", Federal Crop Insurance Corporation). Total production is taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4).

⁹ Cottonseed payment per pound of actual upland cotton production = total cottonseed expenditures/(total production [bales] * 480 [pounds/per bale]). Total cottonseed payments are listed in Brazil's answer to question 17 (see para. 9). Total production is taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 4).

98. Brazil notes that also under this approach, the total US support to upland cotton in MY 1999-2002 surpasses the support decided by the United States in MY 1992. Brazil furthermore notes that even considering the support programs (and their respective replacements)⁹⁹ individually, nearly all of them provide higher support in MY 1999-2002 than they (or their predecessors) did in MY 1992 (with the exception of Step 2 and PFC / market loss assistance in MY 2001).

61. Does the United States consider that Article 13(b)(ii) permits a comparison on any basis other than a per pound basis? USA

62. According to Prof. Sumner's calculation, the per pound support increased by approximately 24 % from 1992 to 2002. On the other hand, the Panel understands that the

⁹⁹ The deficiency payments were replaced by PFC and market loss assistance payments in MY 1999-2001 and by direct and counter-cyclical payments in MY 2002.

total budget outlay, according to Brazil, increased more than that. What, in Brazil's view, is the reason for this difference in the rate of increase? BRA

Brazil's Answer:

99. US budgetary outlays for upland cotton are a function of the level of price, income and other support provided by the US support programmes. Everything being equal, an increase in the "rate of support" as interpreted by the United States would translate one-to-one into an increase of expenditure. However, the "rate of support" is not the only determinant of budgetary outlays, as two important qualifications apply. First, the most important US subsidy programmes for upland cotton are price-based.¹⁰⁰ For instance the marketing loan payment in MY 2002 guarantees a return of 52 cents per pound. With lower market prices, the gap between the adjusted world price and the loan rate, i.e., the basis for the calculation of the marketing loan benefit, widens and payments per pound increase. During the period MY 1992-2001, prices for upland cotton fell drastically.¹⁰¹ For example, average upland cotton prices received by farmers in the United States were 53.7 cents per pound in MY 1992 and dropped to a low of 29.8 cents per pound in MY 2001.¹⁰² Therefore, even for an identical set of programs providing an identical "rate of support," budgetary outlays would have vastly increased due to the drop in prices.

100. Second, the United States increased the production of upland cotton between MY 1992 and MY 1999-2002 from 15.7 million bales in MY 1992 to 16.3 million bales in MY 1999, 16.8 million bales in MY 2000, 19.6 million bales in MY 2001 and 16.7 million bales in MY 2002.¹⁰³ Thus, the increased "rate of support" was applicable to an increased production of upland cotton.

101. In sum, budgetary outlays for upland cotton increased between MY 1992 and MY 2002 for three main reasons: first, the United States increased its "rate of support", second, lower upland cotton prices led to higher budgetary outlays per pound of upland cotton produced; and third, at times of falling market prices, the United States expanded its upland cotton production so that more upland cotton was eligible to receive the increased rate of support. All of this resulted in an increase of budgetary outlays for upland cotton that is relatively bigger than the increase in the US "rate of support".

102. Lastly, Brazil notes that none of the figures presented by Professor Sumner¹⁰⁴ represent actual payments or actual rates of support. Rather, those figures represent average or expected rates of support in any given marketing year. They are not based on actual production or prices,¹⁰⁵ but solely on expected production and prices. Therefore, they cannot easily be compared to actual payments made by the United States in support of upland cotton. Professor Sumner chose the expected support approach in order to match the approach suggested by the United States as closely as possible, while correcting for its simplistic reliance on the target price that disregarded the eligibility criteria and other features of the programmes.

63. In relation to Prof. Sumner's presentation at the first session of the first substantive meeting, please elaborate on the reasons behind the increase in the figures (from 1992 to 2002) concerning Loan Support and Step2 payments. BRA

¹⁰⁰ These include the marketing loan program, the deficiency payment program, the counter-cyclical payment programme and the Step 2 programs.

¹⁰¹ See First Submission of Brazil, para. 28.

¹⁰² Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 5).

¹⁰³ Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4).

¹⁰⁴ See Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting of the Panel).

¹⁰⁵ Which would only be important for the rate of Step 2 payments, as only this programme depends on actual prices for purposes of a rate of support. The other programs reduce Government payments with increasing prices, so that the total rate of support remains basically the same, or are not price-related.

Brazil's Answer:

103. The support rate from the marketing loan programme calculated by Professor Sumner represents the expected support rate from the marketing loan programme. Concerning the marketing loan programme, Brazil notes that the statutory loan rate, indeed, fell from 52.35 cents per pound in MY 1992 to 51.92 cents per pound in MY 1999-2001¹⁰⁶ before being slightly increased in MY 2002 to 52 cents per pound.¹⁰⁷ However, the somewhat higher loan rate in MY 1992 was accompanied by strict eligibility criteria.¹⁰⁸ In MY 1992, only production on farmland that participated in the upland cotton deficiency payment programme was eligible for marketing loan benefits, which restricted eligibility to 84.7 percent of production.¹⁰⁹ In MY 1999-2001, only upland cotton produced on farmland that participated in the PFC programme was eligible. Professor Sumner has conservatively used 97 percent of upland cotton production in MY 1999-2001 as the participation rate of upland cotton.¹¹⁰ Finally, in MY 2002, all US production of upland cotton was eligible to receive marketing loan benefits.¹¹¹ Thus, taking into account the eligibility criteria for benefiting from the marketing loan programme, the slightly higher loan rate in MY 1992 provided less support to total expected US upland cotton production than the slightly lower loan rates in later years.

104. Concerning the difference between the expected Step 2 rate of support in MY 1992-2001 and MY 2002, this difference stems from the fact that the United States eliminated the 1.25 cents per pound threshold for Step 2 payments in the 2002 FSRI Act. Before MY 2002, Step 2 payments were made in the amount of the difference between the A-Index and the lowest priced US quote for upland cotton minus a 1.25 cents per pound threshold. Section 1207(a)(4) of the 2002 FSRI Act postpones the application of this threshold until 1 August 2006.¹¹² Thus, expected Step 2 payments for MY 2002 (and through MY 2005) will be 1.25 cents per pound higher than under the 1990 and 1996 Farm Acts, which both applied the threshold.¹¹³

64. Do the figures cited in Prof. Sumner's presentation at the first session of the first substantive meeting indicate amount available or amount spent? Can the Panel derive amount spent from these figures? If Article 13(b)(ii) requires a rate of support comparison, is the rate of support the "rate" of support available or the "rate" at which the support was spent? BRA

Brazil's Answer:

105. The figures in Professor Sumner's calculation do not indicate amounts spent, but were an attempt to approximate the expected rate of support for an expected pound of upland cotton production under the specific rules in place for each support programme in that year. The figures attempt to represent the normal result that would have been expected by policy makers and farmers as a result of the programme decisions taken by the United States. They do not represent actual expenditures per unit for any programme in any year because, in every year, the actual programme payments per pound of actual production deviates from the expected or normal payments, because the actual production will not exactly equal the expected production.

¹⁰⁶ Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 5).

¹⁰⁷ Exhibit Bra-29 (Section 1202(a)(6) and 1202(b)(6) of the 2002 FSRI Act).

¹⁰⁸ See Exhibit US-3 (7 CFR 1427.4(a)(3) and 7 CFR 1413 (1992 edition)).

¹⁰⁹ Annex 2 to Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting of the Panel, p. 3).

¹¹⁰ Annex 2 to Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting of the Panel, p. 4).

¹¹¹ Exhibit Bra-29 (Section 1201(b) of the 2002 FSRI Act).

¹¹² Exhibit Bra-29 (Section 1207(a)(4) of the 2002 FSRI Act).

¹¹³ See Exhibit Bra-12 ("Cotton: Background for 1995 Farm Legislation", USDA, April 1995, p. 16) and Exhibit Bra-46 ("Cotton: Background and Issues for Farm Legislation," USDA, July 2001, p. 9).

106. For some of the US support programs, the support indicated can be considered – within certain limits – as support available per pound. However, there is not a complete identity between the “expected rate of support” and the “support available to a pound of actual upland cotton production,” because – as noted above – expected and actual production will vary from each other.

107. For marketing loan benefits, the loan rate can be considered the maximum support available to eligible production in case the market price would fall to zero. Similarly, for deficiency and counter-cyclical payments, the difference between the loan rate and the target price can be considered the maximum support available, albeit again only for the eligible production. The expected support differs from that, as it takes into account that not all of the expected production will benefit from those subsidies. The actual support differs again, as expected and actual production may not be identical. Finally, actual US Government payments depend on market prices.

108. For PFC, market loss assistance, direct and cottonseed payments and crop insurance subsidies, the “expected rates of support” represent expected expenditures per unit of expected production. This has been calculated by using average budget expenditures over an appropriate period as expected support, and by using average production as the expected production. Thus, these payments are not maximum available “rates of support”. For example, under the crop insurance programme the US Government pays premium subsidies. Higher per unit support would have been available had all farms joined the programme at the maximum subsidized rates. However, this was not an expected or normal occurrence. Especially in MY 1992, when subsidy rates were relatively low, many upland cotton farms were expected to forgo participation in the programme. Both maximum available crop insurance subsidies as well as expected or normal crop insurance subsidies increased for MY 1999 through 2002, as premium subsidies rose and more cotton acreage found the programme attractive. For crop insurance, but also for PFC and direct payments as well as market loss assistance, the actual support per pound of upland cotton production will vary with the actual production undertaken and actual yields achieved.

109. The actual “rate of support” from the Step 2 payments depends on the actual price differential between the A-Index and the lowest-prices US quote. While it varies from the expected “rate of support” with the actual realization of the price gap, it is not expected to be systematically correlated to the actual level of prices.

110. In sum, it is not possible to derive the amount spent from the “expected rate of support” calculated by Professor Sumner without adding additional information on the level of market prices and the actual US upland cotton acreage, yield and production, among other variables. Following the US approach, Professor Sumner has calculated an expected rate of support that could be characterized as an expected guaranteed revenue. This approach is distinct from an approach looking into actual expenditures, as favoured and advocated by Brazil. In fact, Professor Sumner applied the US approach to a rate of support that would abstract in as far as possible from actual expenditures.

111. Brazil refers the Panel to its answers to questions 60 and 67 for actual expenditures by year, by programme – both per pounds of upland cotton production and as total expenditures for upland cotton.

112. Should the Panel decide that the required test under Article 13(b)(ii) is a “rate of support”, Brazil submits that the relevant rate of support is “expenditures per pound of production”, and thus the “rate” at which support was spent”, as discussed in Brazil’s answer to Question 60.

65. Does Brazil consider that adjustment for inflation is relevant in the context of the comparison under Article 13 (b)(ii) ? BRA

Brazil's Answer:

113. Brazil does not believe that an adjustment for inflation is relevant in the context of the comparison under Article 13(b)(ii). First, there is nothing in the text of Article 13(b)(ii) that provides for such an adjustment. Second, the only provision of the Agreement on Agriculture addressing inflation is Article 18.4, which provides: "In the review process Members should give due consideration to the influence of excessive rates of inflation on the ability of any Member to abide by its domestic support commitments." The "review process" is the review by the Committee on Agriculture of the progress of implementation of commitments as set out in Article 18 of the Agreement on Agriculture. The fact that negotiators explicitly opened the possibility of "giving due consideration to the influence of excessive rates of inflation" in the review process, but not for purposes of Article 13(b)(ii), is evidence that this omission was intentional.

114. Furthermore, at no time during the review process has the United States ever stated or made any notifications that "excessive rates of inflation" in the US economy have negatively impacted "the ability of [the United States] to abide by its domestic support commitments". Even, if it had, Article 18.4 has no relevance for the purposes of the comparison required by Article 13(b)(ii), as it refers to the review process only, and not to the peace clause. Accordingly, there is no basis for the Panel to apply any adjustment to the US level of support to upland cotton in marketing year 1992.

115. Nevertheless, if the Panel should decide to use such an adjustment, Brazil submits that the appropriate index to be used is the applicable US agricultural price index. Three alternative indexes could be used. The first and most direct is the index of prices received for cotton. Other indexes that may be considered are the index of prices received for crops and the index of prices received for all farm products.

	2000	2001	2002
Index of prices received for cotton	82	65	49
Index of prices received for all crops	96	99	103
Index of prices received for all farm products	96	102	99

1990 to 1992 average = 100¹¹⁴

116. Thus, under none of the applicable indices is there any significant inflation to be taken into account. To the contrary, the cotton price index fell by 51 percent, while price indices for crops and all farm products have been stable if compared to the 1990-1992 base used by USDA.

66. Could you please comment on the relative merits of each of the following calculation methods for the purposes of the comparison of support to upland cotton with 1992, irrespective of whether a particular measure should be included or excluded:

- (a) Total budgetary outlays (Brazil's approach). USA**
- (b) Budgetary outlays per unit of upland cotton: Could you please calculate and provide an estimate for the marketing years 1992 and 1999-2002, respectively, and draw attention to any factors/qualifications that the Panel would need to be aware of. BRA, USA**

¹¹⁴ Exhibit Bra-149 (Agricultural Outlook, August 2002, p. 38)

Brazil's Answer:

117. Brazil has presented figures for budgetary outlays by unit of actual production in its answer to Question 60. However, Brazil would like to add some further considerations on the shortcomings of this approach.

118. A significant issue in using these per unit figures to represent support rather than total budgetary outlays is that a per-unit approach discounts the fact that some of the change in production is itself caused by changes in the rate of support or subsidy. If support is calculated by dividing budgetary outlays by total production, the result neglects this effect. As support rises in the numerator, production rises in the denominator and the ratio or per unit of an increased support rate rises by less than total support (and may even decline).

119. The perverse effect is that the more production is stimulated by the US domestic support programmes and, thus, the more those programmes distort trade, the smaller the per unit measure effect of the increased subsidy. For this reason, a subsidy rate per unit of actual production should be avoided or used with extreme caution.

(c) Per unit rate of support (United States approach): How should changes in acreage, eligibility and payment limitations per farm(s) (commodity certificate programmes) be factored into this approach? BRA

Brazil's Answer:

120. The approach of the United States was simply to assert that the target price represented the rate of support per unit in MY 1992 and the loan rate alone represented the rate of support per unit in MY 2002. This approach rests on several fundamental errors.

121. First, the approach left out major support programs in each year. For 1992, the approach left out the Step 2 programme and crop insurance, both of which provided support to upland cotton in that year. For 2002, the approach of the United States left out support provided by the direct payment programme, the counter-cyclical payment programme and the cottonseed payment programme as well as the Step 2 and crop insurance programmes.

122. Second, the United States did not account for any factors that limited eligibility for support or imposed costs of participation as a mandatory condition of receiving support from the US support programmes. The failure to account for these factors in each year completely ignores the true nature of the US support programmes for upland cotton and seriously distorts the rate of support.

123. Lastly, these two per pound numbers cannot simply be added together because the eligibility criteria differ between them and, in particular, the support from the upland cotton deficiency payment programme was expected to apply to an even smaller share of actual production than the support from the marketing loan programme.

124. Professor Sumner's calculation attempted to correct the US presentation for these serious flaws in the implementation of the US approach. Professor Sumner added back the programmes that provide support to upland cotton, but that have been left out by the United States. He also corrected the rate of support for eligibility restrictions and the cost of participation, and presented the rate of support on the basis of expected production in order to be able to sum up the various "rates of support." At the same time, Professor Sumner has attempted to remain true to the approach of the United States by avoiding the use of actual production or actual payments, and instead relying on expected programme support per unit and expected or normal production to arrive at per unit support. Professor Sumner's approach also deals in detail with the question of how to account for eligibility

restrictions and costs of participation. Brazil refers the Panel to Annex 2 to Exhibit Bra-105 for the details of Professor Sumner's methodology.

125. In addition to eligibility, the Panel's question refers specifically to payment limits. Payment limits are applied on the basis of persons, including corporations, partnerships, producers and other persons actively engaged in agriculture.¹¹⁵ Typically, for larger farms, there is more than one person actively engaged in agriculture, including spouses, and landlords on a share rental basis. In addition, there is typically more than one legal entity per farm and under the three entity rule, a person may receive programme payments from three entities and up to double the payment limit for that person for one entity.¹¹⁶

126. Payment limits for deficiency payments in MY 1992 were \$50,000.¹¹⁷ Payment limits for PFC (in MY 1999-2001)¹¹⁸ were \$40,000,¹¹⁹ as is the case for direct payments (in MY 2002).¹²⁰ Payment limits for counter-cyclical payments are \$65,000 (in MY 2002).¹²¹ For the marketing loan programme, a payment limitation of \$75,000 per person applied in MY 1992. In the 1996 FAIR Act, the payment limits for the marketing loan programme was also \$75,000, but was increased to \$150,000 for MY 1999-2001 by supplemental legislation.¹²² The 2002 FSRI Act limits the amount of marketing loan gains and loan deficiency payments to a total of \$75,000 for each producer.¹²³ However, the key change between MY 1992 and MY 1999-2002 was the establishment of the certificate programme in MY 1999,¹²⁴ which effectively eliminated any payment limit for the marketing loan programme.¹²⁵

127. Brazil has no data that would allow it to factor payment limitations into the calculation of an expected rate of support. However, Brazil notes that with the inception of the commodity certificate programme in MY 1999, the limitations imposed by payment limits have – if anything – been relaxed. Additionally, Brazil notes that its approach to Article 13(b)(ii), by comparing total budgetary outlays, takes the budgetary effects of payment limitations into account. For farmers that have reached their payment limit, the US Government incurs no further expenditures, and consequently, the amount of expenditures is lower than it would be absent the payment limit. In that sense, actual expenditures reflect the effects of payment limits.

128. Finally, Brazil notes that Professor Sumner's calculations also do not account for the increase in production or acreage devoted to upland cotton between MY 1992 and MY 2002. Taking this into account by indexing the "expected rate of support" to the level of MY 1992 production – as one

¹¹⁵ Exhibit Bra-33 (7 CFR 1400.1 et seq.).

¹¹⁶ Exhibit Bra-33 (7 CFR 1400.1 et seq.).

¹¹⁷ Exhibit Bra-12 ("Cotton: Background for 1995 Farm Legislation," USDA, April 1995, p. 14).

¹¹⁸ Additional market loss assistance payments were made that did not count towards the PFC payment limit.

¹¹⁹ Professor Sumner has stated in his statement at the first meeting of the Panel that a typical cotton farm with 3000 acres received about \$300,000 in PFC payments per year (*see* Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting of the Panel, p. 22)). This amount results both from the fact that several persons on a farm may be eligible for payment and from the fact that the three-entity rule doubled the payment limit amount a single person could legally receive (for an explanation on the three-entity rule *see* paragraphs 74-76 of the First Submission of Brazil).

¹²⁰ Exhibit Bra-27 (Side by Side Comparison of the 1996 and 2002 Farm Act, USDA, p. 12).

¹²¹ Exhibit Bra-27 (Side by Side Comparison of the 1996 and 2002 Farm Act, USDA, p. 12).

¹²² Exhibit Bra-27 (Side by Side Comparison of the 1996 and 2002 Farm Act, USDA, p. 12).

¹²³ Exhibit Bra-42 (The 2002 Farm Act, Provisions and Implications for Commodity Markets," USDA, November 2002, p. 7).

¹²⁴ Exhibit Bra-42 (The 2002 Farm Act, Provisions and Implications for Commodity Markets," USDA, November 2002, p. 8); Exhibit Bra-29 (Section 1603 of the 2002 FSRI Act).

¹²⁵ The certificate programme is described in detail in paragraphs 75-76 of the First Submission of Brazil.

possible approach to account for the increase in production – would increase the “expected rate of support” for later marketing years, as the amount of US production of upland cotton increased.¹²⁶ The result of the comparison of MY 1992 and MY 1999-2002 support will, however, be the same: The United States’ support to upland cotton in MY 1999-2002 exceeded the support to upland cotton decided in MY 1992 and the US domestic support measures fail to meet the condition in Article 13(b)(ii) for exemption from actions under Articles 5 and 6 of the SCM Agreement and GATT Article XVI:1.

(d) Per unit rate of support for upland cotton (Prof. Sumner's approach at the first session of the first substantive meeting). USA

(67) The Panel requests the parties to calculate and submit estimates of the AMS for upland cotton for marketing years 1992, 1999, 2000, 2001 and 2002. For this purpose the parties are each requested to submit AMS calculations for upland cotton (using the budgetary-outlay/non-price gap methodology employed by the United States in respect of cotton in its DS Notifications (e.g., G/AG/N/USA/43) and using the formats and supporting tables in document G/AG/2) on the same basis as would be the case in calculating a product specific AMS for the purposes of the calculation of the "Total Current AMS" in any year in accordance with the relevant provisions, including as appropriate Article 1(a), (b) and (h), Article 6 and Annex 3 to the Agreement. BRA, USA

Brazil's Answer:

129. Brazil sets forth the following table that summarizes the AMS calculation for upland cotton for marketing years 1992 and 1999-2002. Using the definition of non-product specific support detailed in Brazil's answer to the Panel's Question 40, all of the programmes listed constitute non-exempt direct payments, within the meaning of G/AG/2, providing product-specific support to upland cotton. The table includes all support programs that should have been included in “Supporting Table DS:6”, within the meaning of G/AG/2. To the best of Brazil's knowledge, no other “product-specific” support to upland cotton has been provided by the US Government.

130. Brazil notes that the United States has notified the deficiency payments using the price gap methodology provided for in Annex 3.¹²⁷ Brazil considers it appropriate to follow the US decision and will, therefore, calculate the amount of support to upland cotton provided by the deficiency payment programme by using the “price gap” approach detailed in Annex 3, paragraph 10 and 11. Brazil notes that US budgetary expenditures for MY 1992 for the deficiency programme were \$1,017.4 million.¹²⁸

¹²⁶ Exhibit Bra -4 (“Fact Sheet, Upland Cotton,” USDA, January 2003, p. 4)

¹²⁷ Exhibit Bra -150 (G/AG/N/USA/10)

¹²⁸ Exhibit Bra -4 (“Fact Sheet: Upland Cotton,” USDA, January 2003, p. 6).

AMS For Upland Cotton By Year And Support Programme

Year Programme	1992	1999	2000	2001	2002
	----- \$ million -----				
Deficiency Payments ¹	812.1	none	none	none	none
PFC Payments ²	none	547.8	541.3	453	none
Market Loss Assistance Payments ³	none	545.1	576.2	625.7	none
Direct Payments ⁴	none	none	none	none	485.1
Counter-cyclical Payments ⁵	none	none	none	none	998.6
Marketing loan (Loan gains and LDP) ⁶	743.8	1,545	542	2,506	952
Step Payment ⁷	206.7	421.6	236.1	196.3	317
Crop Insurance ⁸	26.6	169.6	161.7	262.9	194.1
Cottonseed Payment ⁹	none	79	184.7	none	50
Total	1,789.2	3,308.1	2,242.0	4,043.9	2,996.8

Notes

¹ This calculation is based on the price gap formula set forth in para. 10 and 11 of AoA Annex 3. In its notification of marketing year 1995 support (Exhibit Bra-150 (G/AG/N/USA/10, p. 18), the United States that the applied administered price for upland cotton under the deficiency payment programme is \$1,607.169 per ton. The applied administered price (or target price) has been the same in MY 1992 and MY 1995 (Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 5). Therefore, Brazil uses that figure. The external reference price has been notified by the United States to be \$1,275.741 per ton. Paragraph 11 of AoA Annex 3 specifies that the external reference price is based on 1986-1988 averages that have not changed between MY 1992 and MY 1995. Thus, Brazil bases the price-related direct payments from the deficiency payment programme in MY 1992 on the difference between \$1,607.169 per ton and \$1,275.741 per ton (\$331.428 per ton) multiplied by the eligible production, which results from multiplying the eligible upland cotton base acreage and the payment yield. Professor Sumner has calculated the eligible upland cotton base acreage for MY 1992 to be 10.17 million acres, while the payment yield is 531 pounds per acres (Exhibit Bra-105 (Annex 2 to Statement of Professor Daniel Sumner at the First Meeting of the Panel, p. 5-6). Thus, the eligible production is 5,400,270,000 pounds or 2,450,213 metric tons (2204 pounds equal one metric ton). Thus, the amount of deficiency payments in that enters the calculation of total AMS for MY 1992 is 2,450,213 metric tons * \$331.428 per ton = \$812.069 million.

² PFC payment expenditure for upland cotton = total PFC payment expenditure for upland cotton base * (actual upland cotton acreage / PFC upland cotton base acreage). Total PFC payment expenditure for upland cotton is taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 6). This amount has been adjusted by the ratio of upland cotton acres actually planted (Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4)) to upland cotton base acres in the PFC programme (Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)). This adjustment is necessary because only the portion of upland cotton PFC payments that actually benefits acres planted to upland cotton can be considered support to upland cotton.

³ Market loss assistance expenditure for upland cotton = total market loss assistance expenditure for upland cotton base * (actual upland cotton acreage / market loss assistance (i.e., PFC) upland cotton base acreage). Total market loss assistance expenditures for upland cotton is taken from Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 6). This amount has been adjusted by the ratio of upland cotton acres actually planted (Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4)) to upland cotton base acres in the market loss assistance (i.e., PFC) programme (Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)). This adjustment is necessary because only the portion of upland cotton market loss assistance payments that actually benefits acres planted to upland cotton can be considered support to upland cotton.

⁴ Direct payments = total direct payment expenditure for upland cotton base * (actual upland cotton acreage / direct payment upland cotton base acreage). Total direct payments for MY 2002 have been re-estimated from the figure presented by Brazil in its First Submission, para. 59. The new figure is based on the statutory payment rate of 6.67 cents per pound of upland

cotton base multiplied by the direct payment upland cotton base acreage of 16.3 million acres (Brazil has assumed it to be the previous 5-year average as reported by USDA in Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)) multiplied by the direct payment yield of 604 pounds per acre (Brazil has assumed it to be the previous 5-year average as reported by USDA in Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)). Payments are made on 85 percent of base acres. This translates into a total of \$558.17 million. This amount has been adjusted by the ratio of upland cotton acres actually planted Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4) to upland cotton base acres in the direct payment program. This adjustment is necessary because only the portion of upland cotton market loss assistance payments that actually benefits acres planted to upland cotton can be considered support to upland cotton.

⁵ Counter-cyclical payments = total counter-cyclical payment expenditure for upland cotton base * (actual upland cotton acreage / counter-cyclical payment upland cotton base acreage). Total counter-cyclical payments for MY 2002 have been re-estimated from the figure presented by Brazil in its First Submission, para. 69. The new figure is based on the MY 2002 payment rate of 13.73 cents per pound of upland cotton base multiplied by the counter-cyclical payment upland cotton base acreage of 16.3 million acres (Brazil has assumed it to be the previous 5-year average as reported by USDA in Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50)) multiplied by the counter-cyclical payment yield of 604 pounds per acre (Brazil has assumed it to be the previous 5-year average as reported by USDA in Exhibit Bra-142 (Agricultural Outlook, May 2002, p. 50) Brazil notes that this underestimates the payments, as it disregards the yield update for purposes of the counter-cyclical payments). Payments are made on 85 percent of base acres. This translates into a total of \$1148.98 million. This amount has been adjusted by the ratio of upland cotton acres actually planted Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4) to upland cotton base acres in the counter-cyclical payment program. This adjustment is necessary because only the portion of upland cotton market loss assistance payments that actually benefits acres planted to upland cotton can be considered support to upland cotton.

⁶ Total marketing loan payments (marketing loan gains plus loan deficiency payments) are taken para. 144, 148-149 of the First Submission of Brazil.

⁷ Total Step 2 payments are contained in Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 6). Brazil has estimated the MY 2002 amount at note 335 in its First Submission to be \$317 million.

⁸ Total crop insurance payments are taken from Exhibit Bra-57 ("Crop Year Statistics," Federal Crop Insurance Corporation).

⁹ Total cottonseed payments are listed in Brazil's answer to question 17 (see para. 9).

131. The figures presented above indicate that, using the AMS approach, the US level of support for MY 1992 is lower than in each of the marketing years between 1999 and 2002.

132. Brazil also notes that – as explained in the notes on the sources and methodology for arriving at the reported figures – the AMS figures for MY 1999-2002 reflect revised amounts of budgetary expenditures that should replace those listed in Brazil's First Submission at paragraphs 148-149.¹²⁹ These revised (and somewhat smaller) expenditures reflect new information collected by Brazil and more accurately tabulate support to upland cotton in MY 1999-2002. Brazil notes that none of these revisions results in any significant change to the total support to upland cotton, and that expenditures decided in MY 1992 are still well below expenditures related to MY 1999-2002.

68. Could you please clarify the result of the calculations of, and the meaning of the title, in Appendix Table 1 "Estimated per unit Subsidy Rates by Programme and Year" in Annex 2 to Exhibit BRA-105, page 12. Why are the numbers calculated for marketing loans considered to be subsidies? Could the Panel, for example, read the "total level of support" (bottom line of the table) as the effective support price for upland cotton or the maximum rate of support for upland cotton? BRA, USA

Brazil's Answer:

133. The Appendix Table 1 in Annex 2 to Exhibit Bra-105 should have been titled, "Estimated per unit Support Rates by Programme and Year". Brazil apologizes for any confusion caused by mis-titling this table.

134. The marketing loan programme support listed in Table 1 of Annex 2 to Exhibit Bra-105 is a "support rate" and not an actual loan deficiency payment or marketing loan gain. It does not represent a subsidy amount. The loan deficiency payment or marketing loan gain is calculated as the difference between the loan rate and the adjusted world price (AWP). When the AWP falls, the loan benefit per

¹²⁹ No such revision is necessary for MY 1992.

unit of eligible production rises to offset the fall in the AWP. In the US "rate of support" methodology, because the AWP is expected to be positively related to the price received by individual farmers in the United States, the loan rate of 52.35 cents per pound in MY 1992 can be considered an approximate rate of support per unit of eligible production.

135. The deficiency payment rate of support is similar to the marketing loan rate of support and represents the maximum rate of support per eligible unit, where eligibility is measured by the rules applicable in 1992. By contrast, actual support payments under Brazil's expenditure methodology are calculated as the difference between the higher of the average price received by farmers and the loan rate.

136. The other programmes listed in Table 1 provide support per unit of eligible production to upland cotton in addition to the loan rate and deficiency payment target price. These other programmes are calculated as the estimated expected support rates. These rates are not maximum rates of support but rather normal or expected rates of support. The other domestic support measures are not equivalent in overall effect to a price support, but they are calculated on a per unit basis and are added across programmes to give a total support rate.

137. The production and trade distorting effects of these subsidies are each different and are also different from a support price.¹³⁰ Brazil will discuss the adverse effects caused by each of those subsidies in its Further Submission, scheduled for 9 September 2003. The variety of the support programmes employed by the United States precludes interpreting the sum of the various support contributions as a "support price." However, their sum can be read as an expected guaranteed income that results from market revenue and US Government payments. Marketing loan benefits, deficiency payments and counter-cyclical payments will increase with falling market prices. Other support programs are relatively decoupled from market prices, and provide an expected rate of support, that can be added to the loan rate and target price established by the marketing loan, the deficiency and counter-cyclical payments.

69. Can the United States confirm that the "marketing year" for upland cotton is 1 August to 31 July ? Can the United States confirm the Panel's understanding that USDA data for the "crop year" corresponds to the "marketing year"? USA

E. EXPORT CREDIT GUARANTEE PROGRAMMES

70. How does Brazil respond to the United States' assertion that Brazil is trying to realize through litigation what it could not achieve in past negotiations? BRA

Brazil's Answer:

138. In WTO dispute settlement, there is only one way to determine what was achieved in past negotiations – to interpret those provisions actually concluded according to the customary rules of interpretation included in the Vienna Convention. In paragraphs 100-115 of Brazil's Statement at the First Panel Meeting, Brazil demonstrated that it is not in fact attempting "to realize through litigation what it could not achieve in past negotiations." In those paragraphs, Brazil demonstrated that under the ordinary meaning of Article 10.2 of the Agreement on Agriculture, in its context and according to the object and purpose of Article 10 and the Agreement on Agriculture overall, export credit guarantees are subject to the general export subsidy disciplines in the Agreement on Agriculture. Brazil will not repeat those arguments here, but simply notes that by ignoring an interpretation of Article 10.2 according to the Vienna Convention rules, it is the United States that is trying to escape what was in fact achieved in the Uruguay Round negotiations. Other participants in those

¹³⁰ See Exhibit Bra-105 (Statement by Professor Daniel Sumner at the First Meeting of the Panel, paras 20-39) for a summary of the economic impacts of these various support programs.

negotiations who are third parties in this dispute and who in fact use export credits – Canada, the European Communities and New Zealand – agree with Brazil.

- 71. (a) Is an export credit guarantee a financial contribution in the form of a "potential direct transfer of funds or liabilities (e.g. loan guarantee)" within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement? Why or why not? Does it confer a benefit within the meaning of Article 1.1(b)? Why or why not? If so, to whom? USA**

Brazil's Comment:

139. In paragraphs 287-289 of its First Submission, and again at paragraph 116 of its Statement at the First Panel Meeting, Brazil demonstrated that CCC export credit guarantees are expressly included as "financial contributions" within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement. Although export credit guarantees do not automatically confer benefits, CCC export credit guarantees confer "benefits" within the meaning of Article 1.1(b) because they are extended at premium rates and on repayment terms that are not available and in fact do not exist on the market. In its comments and answers to Questions 75 and 82 below, Brazil discusses passages from the GSM 102, GSM 103 and SCGP regulations and materials from USDA's Foreign Agricultural Service (FAS) concerning the programmes, which demonstrate that GSM 102, GSM 103 and SCGP confer "benefits".

140. Brazil notes that a number of agents benefit from the subsidy provided by the guarantees. The US financial institutions and the foreign bank enter into lucrative contracts they would not otherwise have, the importer also gets financing that would not otherwise have been available in the market, but the US Government ultimately designed the programs to provide a benefit to US farmers and exporters. On the FAS website "What Every Exporter Should Know About The GSM-102 and GSM-103 Programmes" it stated that the "USDA will consider announcing, for a specific country or region, the availability of guarantees for any US commercial commodity, if the market for US exports will be expanded or maintained as a result" (emphasis added).¹³¹ Brazil also notes that it is the US exporter who applies for the guarantee and who triggers the process of obtaining coverage for each particular transaction.

- (b) How, if at all, would these elements be relevant to the claims of Brazil, and the United States response thereto? BRA, USA**

Brazil's Answer:

141. Brazil notes that because CCC export credit guarantees constitute subsidies *per se*, and because they are, further, de jure contingent on export, the GSM 102, GSM 103 and SCGP programmes constitute export subsidies within the meaning of Article 3.1(a) of the SCM Agreement. According to the reasoning of the Appellate Body in US – FSC,¹³² this means that those programs are also export subsidies within the meaning of the Agreement on Agriculture. In paragraphs 295-304 of its First Submission, Brazil then demonstrated that those programs threaten to lead to circumvention of the United States' export subsidy commitments (both with respect to scheduled and unscheduled commodities), in violation of Article 10.1 of the Agreement on Agriculture and, as a consequence, of Article 8 of that Agreement. Having established a violation of Part V of the Agriculture Agreement, Brazil's claims under Article 3.1(a) of the SCM Agreement against the CCC export credit guarantee programmes are not exempt from action by Article 13(c)(ii) of the Agreement on Agriculture.

¹³¹ Exhibit Bra-151 ("US Export Credit Guarantee Programs: What Every Exporter Should Know About The GSM-102 and GSM-103 Programmes", USDA, November 1996).

¹³² Appellate Body Report, US – FSC, WT/DS108/AB/R. para. 139-141.

142. Articles 1.1(a)(1)(i) and 1.1(b) of the SCM Agreement are relevant for a number of reasons, including for the purposes of Article 10.3 of the Agreement on Agriculture. As demonstrated in paragraphs 263-268 of Brazil's First Submission, the United States has surpassed its export quantity commitment levels for commodities eligible for GSM 102, GSM 103 and SCGP support. Under Article 10.3, the burden now lies with the United States to prove that its exports in excess of these commitments did not benefit from export subsidies, including export credit guarantees. United States will, inter alia, have to prove that those programs do not grant "benefits" within the meaning of Article 1.1(b) of the SCM Agreement.¹³³

72. Could Brazil expand on why, as indicated in paragraph 118 of its oral statement, it does "not agree" with the United States arguments relating to the viability of an a contrario interpretation of item (j) of the Illustrative List of Export Subsidies in Annex 1 of the SCM Agreement? BRA

Brazil's Answer:

143. As the Panel is aware, Brazil was earlier involved in a dispute (Brazil – Aircraft) that addressed the question whether certain items in the Illustrative List of Export Subsidies admit of an a contrario defense. Although, as the United States notes, Brazil argued in that dispute that a contrario interpretations of certain items included in the Illustrative List (in particular the first paragraph of item (k)) are enabled by footnote 5 to the SCM Agreement, the panel disagreed.

144. Footnote 5 provides that "Measures referred to in Annex I as not constituting export subsidies shall not be prohibited under this or any other provision of this Agreement." The first Article 21.5 panel in Brazil – Aircraft concluded as follows with respect to footnote 5:¹³⁴

6.36 In its ordinary meaning, footnote 5 relates to situations where a measure is referred to as not constituting an export subsidy. Thus, one example of a measure that clearly falls within the scope of footnote 5 involves export credit practices that are in conformity with the interest rate provisions of the Arrangement on Guidelines for Officially Supported Export Credits ("Arrangement"). The second paragraph of item (k) provides that such measures "shall not be considered an export subsidy prohibited by this Agreement". Arguably, footnote 5 in its ordinary meaning could extend more broadly to cover cases where the Illustrative List contains some other form of affirmative statement that a measure is not subject to the Article 3.1(a) prohibition, that it is not prohibited, or that it is allowed, such as, for example, the first and last sentences of footnote 59³⁴ and the proviso clauses of items (h)³⁵ and (i)³⁶ of the Illustrative List.³⁷

6.37 The first paragraph of item (k), however, does not contain any affirmative statement that a measure is not an export subsidy nor that measures not satisfying the conditions of that item are not prohibited. To the contrary, the first paragraph of item (k) on its face simply identifies measures that are prohibited export subsidies. Thus, the first paragraph of item (k) on its face does not in our view fall within the scope of footnote 5 read in conformity with its ordinary meaning.

³⁴ The first sentence of footnote 59 provides that "Members recognize that deferral need not amount to an export subsidy where, for example, appropriate interest charges are collected." The last sentence states that "[p]aragraph (e) is not intended to limit a Member from taking measures to avoid the double taxation of foreign-source income earned by its enterprises or the enterprises of another Member."

¹³³ The United States will also have to prove that the programmes are not inconsistent with item (j) of the Illustrative List of export subsidies.

¹³⁴ Panel Report, *Brazil – Aircraft (21.5)*, WT/DS46/RW, paras. 6.36-6.37.

³⁵ “. . . provided, however, that prior-stage cumulative indirect taxes may be exempted, remitted or deferred on exported products even when not exempted, remitted or deferred on like products sold for domestic consumption, if the prior stage cumulative indirect taxes are levied on inputs that are consumed in the production of the exported product . . .” (emphasis added).

³⁶ “. . . provided, however, that in particular cases a firm may use a quantity of home market inputs equal to, and having the same quality and characteristics as, the imported inputs as a substitute for them . . .”

³⁷ In any event, such measures may well fall within the scope of footnote 1, and thus not represent subsidies at all, whether prohibited or otherwise.

145. Reflecting on footnote 5, the panel recalled and rejected the US argument that “[t]he Illustrative List does not deal with all possible financial contributions, but for those it does deal with, it establishes, by virtue of footnote 5, a dispositive legal standard insofar as prohibited subsidies are concerned”.¹³⁵ While the panel agreed that “an illustrative list could in principle operate in such a manner”, it concluded that because of footnote 5, the Illustrative List of Export Subsidies annexed to the SCM Agreement did not operate in that manner.¹³⁶ According to the panel, “if the drafters had intended the meaning which the United States attributes to footnote 5, they could certainly have found appropriate language to do so”.¹³⁷

146. The panel noted that the first paragraph of item (k) has effect even if it does not admit of an a contrario interpretation. The panel likened the Illustrative List to “a list of per se violations”.¹³⁸ According to the panel, even if a measure does not fulfill the elements of one of the items in the Illustrative List and therefore does not constitute a per se violation, it could still be deemed prohibited if the complaining party demonstrates that it fulfills the elements of Articles 1 and 3 of the SCM Agreement.¹³⁹

147. In dicta, the Appellate Body suggested that the first paragraph of item (k) may indeed admit of an a contrario interpretation.¹⁴⁰ In Brazil’s view, however, this suggestion is limited to the first paragraph of item (k), and at least does not extend to item (j). Although the Appellate Body emphasized in the initial appeal in *Brazil – Aircraft* that the term “material advantage” in item (k) had to be given meaning independent of the term “benefit” in Article 1.1(b)¹⁴¹, it found that the difference between the two terms is the qualification in item (k) that the advantage conferred relative to the market must additionally be “material”.¹⁴² In other words, proving “material advantage” includes a showing that a “benefit” is conferred, but also requires something more. While disproving the existence of a “material advantage” may mean that, in some narrow circumstances, a benefit may nevertheless still exist, the first paragraph of item (k) at least still relies on an analysis whether a “material advantage” is conferred to the recipient, as compared to some market benchmark. This “to the recipient” standard does not undercut and in fact complements the market benchmark “to the recipient” standard included in Article 1.1(b). An a contrario reading of item (k), therefore, does not read out the market benchmark “to the recipient” standard from the test applicable to export credits, but simply gives it a particular meaning in the context of export credits.

¹³⁵ Panel Report, *Brazil – Aircraft* (21.5), WT/DS46/RW, paras. 6.32, 6.38.

¹³⁶ Panel Report, *Brazil – Aircraft* (21.5), WT/DS46/RW, para. 6.38.

¹³⁷ Panel Report, *Brazil – Aircraft* (21.5), WT/DS46/RW, para. 6.38.

¹³⁸ Panel Report, *Brazil – Aircraft* (21.5), WT/DS46/RW, para. 6.42.

¹³⁹ Panel Report, *Brazil – Aircraft* (21.5), WT/DS46/RW, para. 6.42.

¹⁴⁰ Appellate Body Report, *Brazil – Aircraft* (21.5), WT/DS46/AB/RW (adopted 4 August 2000), para. 80 (“If Brazil had demonstrated that the payments made under the revised PROEX were not ‘used to secure a material advantage in the field of export credit terms’, and that such payments were ‘payments’ by Brazil of ‘all or part of the costs incurred by exporters or financial institutions in obtaining credits’, then we would have been prepared to find that the payments made under the revised PROEX are justified under item (k) of the Illustrative List.”).

¹⁴¹ Appellate Body Report, *Brazil – Aircraft*, WT/DS46/AB/R, para. 179.

¹⁴² Appellate Body Report, *Brazil – Aircraft*, WT/DS46/AB/R, para. 177.

148. In contrast, the evidence required to meet the elements of item (j) are completely unrelated to the evidence necessary to establish that a guarantee programme confers a benefit “to the recipient” of a loan guarantee. Whether the premia collected under an export credit guarantee programme meet the long-term operating costs and losses of the programme is completely irrelevant to the question whether a benefit “to the recipient” of the export credit guarantee is conferred. Consequently, allowing an a contrario reading of item (j) that provides, as the United States argues, “a dispositive legal standard”¹⁴³ for determining whether guarantees are prohibited, would suggest that the “to the recipient” market benchmark standard does not apply to guarantees. This cannot be true, since guarantees are expressly included in Article 1.1 (and Article 14(c)) as “financial contributions” that can confer “benefits” to a recipient relative to a market benchmark.

149. The conclusion that item (j) does not admit of an a contrario defense is relevant for a number of reasons, including for the purposes of Article 10.3 of the Agreement on Agriculture. As demonstrated in paragraphs 263-268 of Brazil’s First Submission, the United States has surpassed its export quantity commitment levels for commodities eligible for GSM 102, GSM 103 and SCGP support. Under Article 10.3, the burden now lies with the United States to prove that its exports in excess of these commitments did not benefit from export subsidies, including export credit guarantees. Even if the United States is able to demonstrate that premia for the GSM 102, GSM 103 and SCGP programs meet long-term operating costs and losses, it will also have to prove that those programs do not grant “benefits” within the meaning of Article 1.1(b) of the SCM Agreement. Since item (j) does not admit of an a contrario interpretation, disproving the elements of item (j) will not be sufficient to remove the programs from the definition of “export subsidy.”

73. The Panel could arguably take the view that Articles 1 and 3 of the SCM Agreement were relevant in assessing the WTO-consistency of United States export credit guarantees. The United States has yet to submit any evidence or argumentation on this point, either as potential context for interpretation of the terms in Article 10 of the Agreement on Agriculture or in relation to Brazil's claims under the SCM Agreement. The Panel would therefore appreciate United States views in respect of this situation, and invites the United States to submit relevant argumentation and evidence. USA

74. If the Panel decides to refer to provisions of the SCM Agreement for contextual guidance in the interpretation of the terms in Article 10 of the Agreement on Agriculture, should the Panel refer to item (j) or Articles 1 and 3 of the SCM Agreement or both? BRA, USA

Brazil’s Answer:

150. In determining what constitutes an export subsidy within the meaning of Article 10.1 of the Agreement on Agriculture, Brazil considers that the Panel should refer to contextual guidance included in Articles 1 and 3 of the SCM Agreement, and in item (j) of the Illustrative List of Export Subsidies annexed to the SCM Agreement. As discussed in paragraphs 258-261 of Brazil’s First Submission, this is consistent with the Appellate Body’s decisions in US – FSC¹⁴⁴ and Canada – Dairy.¹⁴⁵ As a factual matter, Brazil has demonstrated that the GSM 102, GSM 103 and SCGP programmes constitute export subsidies under Articles 1.1 and 3.1(a) of the SCM Agreement, and under item (j) of the Illustrative List (as well as under Articles 1(e) and 10.1 of the Agreement on Agriculture.

75. The Panel's attention has been drawn to Article 14(c) of the SCM Agreement (see e.g. written third party submission of Canada) and to the panel report in DS 222 Canada- Export Credits and Loan Guarantees. How and to what extent are Article 14(c) of the SCM

¹⁴³ Panel Report, *Brazil – Aircraft* (21.5), WT/DS46/RW, para. 6.32

¹⁴⁴ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 136-140.

¹⁴⁵ Appellate Body Report, *Canada – Dairy*, WT/DS103/AB/R and WT/DS113/AB/R, para. 87-90.

Agreement, and the cited panel report, relevant to the issue of whether or not the United States export credit guarantee programmes confer a "benefit"? What would be the appropriate market benchmark to use for any comparison? Please cite any other relevant material. BRA, USA

Brazil's Answer:

151. As one way of demonstrating that the GSM 102, GSM 103 and SCGP programs constitute export subsidies within the meaning of Article 10.1 of the Agreement on Agriculture, Brazil has demonstrated that those programmes constitute financial contributions that confer benefits and that are contingent on export, within the meaning of Articles 1.1 and 3.1(a) of the SCM Agreement. Brazil recalls that as discussed above in response to Question 72, Article 10.3 of the Agreement on Agriculture in fact places the burden on the United States to prove that export quantities in excess of its export commitments have not benefited from export subsidies.

152. In any event, Brazil has demonstrated that the CCC guarantee programs confer "benefits" within the meaning of Article 1.1(b) because they are extended at premium rates and on repayment terms that are not available on the market. In fact, the CCC programmes are unique financing vehicles for agricultural commodity transactions that are not available on the commercial market.

153. Brazil notes that the United States has argued in *Canada – Aircraft II* that where there is no comparable financial product on the market, a programme confers benefits per se. It stated:

If the commercial market does not offer a particular borrower the exact terms offered by a government, then the government is providing a benefit to the recipient whenever those terms are more favorable than the terms that are available in the market. A government entity "operating on commercial principles" is still a government entity. It is not the commercial market.¹⁴⁶

154. Brazil agrees with the United States. This interpretation is, in fact, consistent with the benchmark established by Article 14(c) of the SCM Agreement. In relevant part, Article 14 provides as follows:

For the purposes of Part V, any method used by the investigating authority to calculate the benefit to the recipient ... shall be transparent and adequately explained. Furthermore, any such method shall be consistent with the following guidelines:

...

(c) a loan guarantee by a government shall not be considered as conferring a benefit, unless 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. In this case the benefit shall be the difference between these two amounts adjusted for any differences in fees.

155. Brazil first draws the Panel's attention to the fact that Article 14 was specifically conceived for the purposes of Part V of the SCM Agreement only. It should be referred to exclusively as context to determine whether a benefit exists when a particular transaction is backed by a government export credit guarantee. Secondly, Brazil observes that subparagraph (c) of Article 14 is simply a

¹⁴⁶ Panel Report, *Canada – Aircraft II*, WT/DS222/R, Annex C-2 (para. 7).

“guideline”, not the sole method of calculating the benefit to the recipient. Other methods may be applied as long as they are “consistent” with the guideline set out in subparagraph (c).

156. There is no market benchmark in the case of the GSM 102, GSM 103 and SCGP programmes, since there are no financial products available on the market on the terms provided by the programmes. As discussed in response to Question 82, the regulations regarding the GSM 102 and GSM 103 programmes, as well as regarding the SCGP programme note that “[t]he programs operate in cases where credit is necessary to increase or maintain US exports to a foreign market and where US financial institutions would be unwilling to provide financing without CCC’s guarantee”.¹⁴⁷ Moreover, the regulations state that “[t]he programs are targeted towards those countries where the guarantee is necessary to secure financing of the export but which have sufficient financial strength so that foreign exchange will be available for scheduled payments.”¹⁴⁸ These passages prove that without a CCC guarantee, a borrower would not be able to secure financing at all – not just financing on less attractive terms than could be secured with the CCC guarantee (or on terms that would constitute a benefit under Article 14(c) of the SCM Agreement) – but no financing at all. The regulations also emphasize that the CCC guarantee is necessary – a commercial guarantee would not be sufficient.

157. Moreover, as the FAS website explains, “[t]he reduction of risk to financial institutions in the United States ... may make possible financing that would otherwise be unavailable”.¹⁴⁹ The FAS further clarifies that “a CCC guarantee can encourage extension of credit in cases where financial institutions might otherwise be unwilling to finance export on credit terms”.¹⁵⁰ In addition, the FAS points out that such guarantees would “facilitate credit to foreign banks in larger amounts and on more favorable commercial terms than would otherwise be available”.¹⁵¹ Whatever the meaning of Article 14(c), the provision by CCC of guarantees that do not exist on the market entails the provision of a benefit per se. The benefit to the recipient, under the benchmark established by Article 14(c), would be the total amount of the loan backed by the guarantee, since there would be no “comparable commercial loan absent the government guarantee”.

76. How does the United States respond to Brazil's statement that : "...export credit guarantees for exports of agricultural exports [sic] are not available on the marketplace by commercial lenders"? USA

77. How does the United States interpretation of "long term operating costs and losses" in item (j) as claims paid give meaning to both "costs" and "losses"? Do claims paid represent "losses" or "costs" or both? If claims paid is represented by "losses", what would go into the "cost" element of item (j)? Could the United States expand on why it disagrees with the items which Brazil identifies for inclusion in the examination to be conducted under item (j)? USA

Brazil’s Comment:

158. Brazil may wish to comment in its rebuttal submission on the response the United States ultimately provides to this question. In the meantime, however, Brazil would like to comment on US criticisms of the initial formula Brazil constructed to determine whether the GSM 102, GSM 103 and SCGP programmes fail to meet their long-term operating costs and losses, within the meaning of

¹⁴⁷ Exhibit Bra-38 (7 CFR 1493.10(a)(2)) and Exhibit Bra-38 (7 CFR 1493.400(a)(2)).

¹⁴⁸ Exhibit Bra-38 (7 CFR 1493.10(a)(2)) and Exhibit Bra-38 (7 CFR 1493.400(a)(2)).

¹⁴⁹ Exhibit Bra-151 (“US Export Credit Guarantee Programs: What Every Exporter Should Know About The GSM-102 and GSM-103 Programs,” USDA, November 1996).

¹⁵⁰ Exhibit Bra-151 (“US Export Credit Guarantee Programs: What Every Exporter Should Know About The GSM-102 and GSM-103 Programs,” USDA, November 1996).

¹⁵¹ Exhibit Bra-151 (“US Export Credit Guarantee Programs: What Every Exporter Should Know About The GSM-102 and GSM-103 Programs,” USDA, November 1996).

item (j). The Panel will recall that Brazil's initial formula, which was included in paragraph 281 and Figure 20 of its First Submission, can be stated as follows:

$$\text{Premiums collected} - (\text{Administrative expenses} + \text{Default claims} + \text{Interest expenses})$$

159. Where this formula yields a negative number over a period constituting the "long term", Brazil argued that loan guarantees are provided "at premium rates which are inadequate to cover the long-term operating costs and losses of the programme", within the meaning of item (j).¹⁵² Applying this formula to data for the period 1994-2003, Brazil demonstrated that premiums collected for the CCC guarantee programmes were indeed inadequate to cover operating costs and losses for the programmes.

160. To correct for alleged errors in Brazil's initial constructed formula, which was included in paragraph 281 and Figure 20 of its First Submission, the United States adopted its own alternative formula, in paragraph 173 of its First Submission, which can be stated as follows:

$$(\text{Fees} + \text{Claims recovered} + \text{Claims rescheduled}) - \text{Claims paid}$$

161. Where this formula yields a positive number over a period constituting the "long term," the United States asserts that loan guarantees are provided at premium rates that are adequate to cover the long-term operating costs and losses of the program, within the meaning of item (j).

162. Brazil made several criticisms of the US formula. In paragraph 123 of its Statement at the First Panel Meeting, Brazil demonstrated that the failure to account for interest paid by the CCC to the Treasury Department leads to artificially low accounting of operating costs. In paragraph 122, Brazil additionally demonstrated that it is incorrect to treat rescheduled debt as a recovery of a default claim. Brazil notes that rescheduling can in fact have the effect of increasing the costs incurred by the government, rather than reducing those costs. In its budget documents, the US Government treats Paris Club rescheduling of imminent defaults as "work-outs."¹⁵³ According to the US Office of Management and Budget ("OMB"), work-outs can either have a negative or a positive effect on cash flow.¹⁵⁴ The U. General Accounting Office ("GAO") has in fact stated that historically, the majority of GSM support that is rescheduled is "in arrears."¹⁵⁵ If anything, this increases CCC's cost.

¹⁵² Revenue for "premiums collected" is recorded in the "Financing Account" section of the CCC budget, in the row titled "Loan origination fee" (line 88.40). See the US budget documents included as Exhibits Bra-88 to Bra-95. "Administrative expenses" are recorded in the "Programme Account" section of the CCC budget, in the row titled "Administrative expenses" (line 00.09). See the US budget documents included as Exhibits Bra-88 to Bra-95. Expenses for "default claims" are recorded in the "Financing Account" section of the CCC budget, in the row titled "Default claims" (line 00.01). See the US budget documents included as Exhibits Bra-88 to Bra-95. "Interest expenses" are recorded in the "Financing Account" section of the CCC budget, in the row titled "Interest on debt to Treasury" (line 00.02). See the US budget documents included as Exhibits Bra-88 to Bra-95.

¹⁵³ Exhibit Bra-121 (US General Accounting Office ("GAO"), Report to Congressional Committees, *Credit Reform: US Needs Better Method for Estimating Cost of Foreign Loans and Guarantees*, GAO/NSIAD/GGD-95-31, December 1994, p. 63) ("GAO/NSIAD/GGD-95-31").

¹⁵⁴ Exhibit Bra-116 (Executive Office of the President, Office of Management and Budget, Circular No. A-11, Part 5, *Federal Credit Programs* (June 2002), p. 185-13) ("OMB Circular A-11").

¹⁵⁵ Exhibit Bra-152 (GAO, Statement of Allan I. Mendelowitz, Director, Trade, Energy and Finance Issues, National Security and International Affairs Division, before the Task Force on Urgent Fiscal Issues of the Committee on Budget of the US House of Representatives, *Status Report on GAO's Reviews of the Targeted Export Assistance Program, the Export Enhancement Programme, and the GSM-102/103 Export Credit Guarantee Programmes*, GAO/T-NSIAD-90-53, 28 June 1990, p. 14).

163. The United States' formula did correct for one shortcoming of Brazil's initial constructed formula, however. The United States is correct that Brazil's formula did not include recoveries.¹⁵⁶ Brazil therefore introduces a revised constructed formula that accounts for recoveries and interest on those recoveries, as recorded in the "Principal collections" and "Interest collections" rows¹⁵⁷ of the US budget. It also accounts for the interest accruing to the CCC on balances maintained in its so-called "financing account" for the purposes of potential claims,¹⁵⁸ as recorded in the "Interest on uninvested funds" row of the US budget documents.¹⁵⁹ Brazil's revised constructed formula can be stated as follows (including references to the specific budget lines involved):

(Premiums collected + Recovered principal and interest (Line 88.40) + Interest revenue (Line 88.25)) – (Administrative expenses (Line 00.09) + Default claims (Line 00.01) + Interest expense (Line 00.02))

164. Brazil emphasizes that it does not intend for this revised constructed formula to replace the formula used by the US government itself to track the costs of the CCC guarantee programs, pursuant to the US Federal Credit Reform Act ("FCRA"). In paragraphs 124-133 of its Statement at the First Panel Meeting, Brazil discussed the FCRA cost formula in considerable detail. The chart included at paragraph 132 of Brazil's Statement demonstrates that under the FCRA cost formula, CCC's export credit guarantee programs are offered at premium rates that are inadequate to cover their long-term operating costs and losses. Brazil believes that the FCRA cost formula is one very useful way to determine the performance of the CCC guarantee programs relative to the elements of item (j). However, if the Panel would like to confirm the results of the FCRA cost formula, or refer to an alternative formula, Brazil offers its revised constructed formula for these purposes.

165. Where Brazil's revised constructed formula indicates a net cost over a period constituting the "long term", export credit guarantees are provided "at premium rates which are inadequate to cover the long-term operating costs and losses of the programme", within the meaning of item (j). The following chart demonstrates that during the ten-year period FY 1993-2002, premiums for GSM 102, GSM 103 and SCGP export credit guarantees have been inadequate to cover long-term operating costs and losses. Net costs for the programmes during this period total more than \$1 billion as set forth below:

Fiscal year	Premiums collected (88.40) + Recovered principal and interest (88.40) + Interest revenue (88.25)	Admin. expenses (00.09) + Default claims (00.01) + Interest expense (00.02)
1993	\$27,608,000 + \$12,793,000 + \$15,672,000 ¹⁶⁰ = \$56,073,000	\$3,320,000 ¹⁶¹ + \$570,000,000 ¹⁶² + \$0 ¹⁶³ = \$573,320,000
1994	\$20,893,000 + \$458,954,000 + \$0 ¹⁶⁴ = \$479,847,000	\$3,381,000 ¹⁶⁵ + \$422,363,000 ¹⁶⁶ + \$0 ¹⁶⁷ = \$425,744,000

¹⁵⁶ First Submission of the United States, para. 173.

¹⁵⁷ In combination with loan origination fees, these rows are collectively recorded as line 88.40 in the US budget documents.

¹⁵⁸ Exhibit Bra-116 (OMB Circular A-11, p. 185-51). See also Exhibit Bra-118 (Federal Accounting Standards Advisory Board, *Statement of Federal Financial Accounting Standards No. 19, Technical Amendments to Accounting Standards for Direct Loans and Loan Guarantees in STATEMENT OF FEDERAL FINANCIAL ACCOUNTING STANDARDS NO. 2*, March 2001, p. 16 (para. 37)).

¹⁵⁹ This row is recorded as line 88.25 in the US budget documents. The payment of interest to an agency for uninvested balances in financing accounts is addressed in Exhibit Bra-117 (2 U.S.C. § 661d(c)).

¹⁶⁰ Exhibit Bra-126 (US budget for FY 1995, p. 156).

¹⁶¹ Exhibit Bra-126 (US budget for FY 1995, p. 156).

¹⁶² Exhibit Bra-126 (US budget for FY 1995, p. 156).

¹⁶³ No budget line Exhibit Bra-126 (US budget for FY 1995, p. 156).

¹⁶⁴ Exhibit Bra-95 (US budget for FY 1996, p. 162).

¹⁶⁵ Exhibit Bra-95 (US budget for FY 1996, p. 161).

¹⁶⁶ Exhibit Bra-95 (US budget for FY 1996, p. 162).

1995	\$18,000,000 + \$62,000,000 + \$0 ¹⁶⁸ = \$80,000,000	\$3,000,000 + \$551,000,000 + \$10,000,000 ¹⁶⁹ = \$564,000,000
1996	\$20,000,000 + \$68,000,000 + \$26,000,000 ¹⁷⁰ = \$114,000,000	\$3,000,000 ¹⁷¹ + \$202,000,000 ¹⁷² + \$61,000,000 ¹⁷³ = \$266,000,000
1997	\$14,000,000 + \$104,000,000 + \$26,000,000 ¹⁷⁴ = \$144,000,000	\$4,000,000 ¹⁷⁵ + \$11,000,000 ¹⁷⁶ + \$62,000,000 ¹⁷⁷ = \$77,000,000
1998	\$17,000,000 + \$81,000,000 + \$54,000,000 ¹⁷⁸ = \$152,000,000	\$4,000,000 ¹⁷⁹ + \$72,000,000 ¹⁸⁰ + \$62,000,000 ¹⁸¹ = \$138,000,000
1999	\$14,000,000 + \$58,000,000 + \$0 ¹⁸² = \$72,000,000	\$4,000,000 ¹⁸³ + \$244,000,000 + \$62,000,000 ¹⁸⁴ = \$310,000,000
2000	\$16,000,000 + \$100,000,000 + \$99,000,000 ¹⁸⁵ = \$215,000,000	\$4,000,000 ¹⁸⁶ + \$208,000,000 ¹⁸⁷ + \$62,000,000 ¹⁸⁸ = \$274,000,000
2001	\$18,000,000 + \$149,000,000 + \$125,000,000 ¹⁸⁹ = \$292,000,000	\$4,000,000 ¹⁹⁰ + \$52,000,000 ¹⁹¹ + \$104,000,000 ¹⁹² = \$160,000,000
2002	\$21,000,000 + \$155,000,000 + \$61,000,000 ¹⁹³ = \$237,000,000	\$4,000,000 ¹⁹⁴ + \$40,000,000 ¹⁹⁵ + \$93,000,000 ¹⁹⁶ = \$137,000,000
Total	\$1,841,920,000	\$2,925,064,000
Long-term Net Cost		\$1,083,144,000

166. To arrive at this result, Brazil notes that it did not rely on “estimates” of the programmes’ costs.¹⁹⁷ The annual US budget documents upon which Brazil relied track CCC data for three consecutive years – the prior year, the current year and the budget year. The 2004 budget, for example, which is completed in 2003, includes data for 2002, 2003 and 2004. Budget year data is

¹⁶⁷ Exhibit Bra -95 (US budget for FY 1996, p. 162).

¹⁶⁸ Exhibit Bra -94 (US budget for FY 1997, p. 176).

¹⁶⁹ Exhibit Bra -94 (US budget for FY 1997, p. 175).

¹⁷⁰ Exhibit Bra -93 (US budget for FY 1998, p. 175).

¹⁷¹ Exhibit Bra -93 (US budget for FY 1998, p. 174).

¹⁷² Exhibit Bra -93 (US budget for FY 1998, p. 175).

¹⁷³ Exhibit Bra -93 (US budget for FY 1998, p. 175).

¹⁷⁴ Exhibit Bra -92 (US budget for FY 1999, p. 106).

¹⁷⁵ Exhibit Bra -92 (US budget for FY 1999, p. 105).

¹⁷⁶ Exhibit Bra -92 (US budget for FY 1999, p. 106).

¹⁷⁷ Exhibit Bra -92 (US budget for FY 1999, p. 106).

¹⁷⁸ Exhibit Bra -91 (US budget for FY 2000, p. 112).

¹⁷⁹ Exhibit Bra -91 (US budget for FY 2000, p. 111).

¹⁸⁰ Exhibit Bra -91 (US budget for FY 2000, p. 112).

¹⁸¹ Exhibit Bra -91 (US budget for FY 2000, p. 112).

¹⁸² Exhibit Bra -90 (US budget for FY 2001, p. 112).

¹⁸³ Exhibit Bra -90 (US budget for FY 2001, p. 110).

¹⁸⁴ Exhibit Bra -90 (US budget for FY 2001, p. 111).

¹⁸⁵ Exhibit Bra -89 (US budget for FY 2002, p. 118).

¹⁸⁶ Exhibit Bra -89 (US budget for FY 2002, p. 116).

¹⁸⁷ Exhibit Bra -89 (US budget for FY 2002, p. 117).

¹⁸⁸ Exhibit Bra -89 (US budget for FY 2002, p. 117).

¹⁸⁹ Exhibit Bra -88 (US budget for FY 2003, p. 120).

¹⁹⁰ Exhibit Bra -88 (US budget for FY 2003, p. 118).

¹⁹¹ Exhibit Bra -88 (US budget for FY 2003, p. 119).

¹⁹² Exhibit Bra -88 (US budget for FY 2003, p. 120).

¹⁹³ Exhibit Bra -127 (US budget for FY 2004, p. 109).

¹⁹⁴ Exhibit Bra -127 (US budget for FY 2004, p. 107).

¹⁹⁵ Exhibit Bra -127 (US budget for FY 2004, p. 108).

¹⁹⁶ Exhibit Bra -127 (US budget for FY 2004, p. 108).

¹⁹⁷ First Submission of the United States, paras. 175-178.

indeed based on estimates. Current year data is revised to account for any change to the cost or revenue item at issue. Since the current year is not yet complete when the budget is issued, however, current year data remains, at least in part, based on estimates. Prior year data, however, is based on actual costs and revenues. In applying its formula, Brazil used the data in the prior year column, and therefore used actual costs and revenues, rather than estimates.¹⁹⁸

167. Several other factors corroborate the fact that the CCC export guarantee programmes do not charge premia that allow them to meet their long-term operating costs and losses.

- First, in audit reports of the CCC's fiscal year 2000 and 2001 financial statements, the US Department of Agriculture's Office of the Inspector General noted that "the fees CCC charges for its GSM-102 and GSM-103 export credit guarantee programs have not been changed in 7 years and may not be reflecting current costs."¹⁹⁹ While Brazil does not have fee schedules for the entire period 1993-2002, it provides for the Panel's review fee schedules for GSM 102 and GSM 103 from November 1994, 4 September 2001 and 24 September 2002.²⁰⁰ According to CCC's website, the latter is the fee schedule that is currently in force. The Panel will note that between November 1994 and 23 September 2002, CCC made only one change in its fee schedule for GSM 102: while the fee for a 12-month guarantee with semi-annual repayment intervals was \$0.209 per \$100 of coverage in November 1994, by 4 September 2001 it had changed to \$0.229 per \$100 of coverage. On 24 September 2002, one additional change was made: borrowers were offered the additional option of 30 and 60 day guarantees, at the same fee charged for 90-day and 4-, 6- and 7-month guarantees.
- Second, US Department of Agriculture Under Secretary August Schumacher testified to Congress in 1998 that the GSM 102 programme suffered nearly \$2 billion in losses as a result of Iraqi defaults, and an additional nearly \$2 billion resulting from Polish defaults.²⁰¹ GAO stated that liabilities on the Iraqi debt accrued over the period 1990-1997, as the guaranteed Iraqi borrowings came due.²⁰² As noted by Brazil in paragraph 284 of its First Submission, however, the maximum in GSM 102 premiums the United States could have generated from all export credit guarantees provided during the lifetime of the programmes up to 1998 – had it applied the highest possible

¹⁹⁸ Of the 1994-2003 period tracked in Figure 20 to Brazil's First Submission, the only figures that reflected estimates were those for the year 2003, since actual data is not yet available for that year. To correct this, and to ensure that the data is still sufficient to reveal whether the CCC export credit guarantee programmes incur "long term" operating costs and losses, the chart above tracks CCC guarantees for the period 1993-2002.

¹⁹⁹ Exhibit Bra-153 (US Department of Agriculture Office of Inspector General Financial and IT Operations Audit Report of the Commodity Credit Corporation's Financial Statements for Fiscal Year 2000, Audit Report No. 06401-14-FM (June 2001), p. 31). *See also* Exhibit Bra-154 (US Department of Agriculture Office of Inspector General Great Plains Region Audit Report of the Commodity Credit Corporation's Financial Statements for Fiscal Year 2001, Audit Report No. 06401-4-KC (February 2002), p. 49 ("[T]he fees CCC charged for its GSM-102 and GSM-103 export credit guarantee programmes have not been changed for many years and may not be reflecting current costs.").

²⁰⁰ Exhibit Bra-155 (US Department of Agriculture Foreign Agricultural Service, *Notice to GSM-102 and GSM-103 Programme Participants*, 24 September 2002); Exhibit Bra-98 (US Department of Agriculture Foreign Agricultural Service, *Notice to GSM-102 & GSM-103 Programme Participants*, 4 September 2001); Exhibit Bra-156 (US Export-Import Bank, *Comparison of Major Features of Programmes Offered by Ex-Im Bank and Commodity Credit Corporation for Support of Bulk Agricultural Commodities*, available at <http://www.exim.gov/pub/ins/pdf/eib99-13.pdf>). Brazil was unable to locate from public sources other fee schedules from the period 1993-2002.

²⁰¹ Exhibit Bra-87 ("Testimony of August Schumacher Jr., Under Secretary, Farm and Foreign Agricultural Service, USDA, before the Subcommittee on General Farm Commodities, Hearing on the Asian Financial Crisis, 4 February 1998", p. 10-11).

²⁰² Exhibit Bra-157 (US General Accounting Office, REPORT TO THE CHAIRMAN, TASK FORCE ON URGENT FISCAL ISSUES, COMMITTEE ON THE BUDGET, HOUSE OF REPRESENTATIVES, *International Trade: Iraq's Participation in US Agricultural Export Programs*, GAO/NSIAD-91-76 (November 1990), p. 27 (Table IV.2)).

premium rate to all guarantees – is \$358.54 million.²⁰³ The total amount of received applications for GSM 102 export credit guarantees for the period 1999-2002 was \$11.77 billion, resulting in a theoretical additional maximum premium of \$78.08 million for that period.²⁰⁴ Thus, the highest amount of premiums the United States could have generated under this programme from its inception through 2002 would amount to \$436.62 million.²⁰⁵ This does not come close to covering the programme's losses from the Iraqi and Polish defaults alone.

- Third, CCC financial statements for fiscal year 2002 report that uncollectible amounts on post-1991 CCC guarantees total \$770 million.²⁰⁶ As noted in the chart above at paragraph 165, CCC collected premiums of \$222.641 million for GSM 102, GSM 103 and SCGP during the period 1992-2002.²⁰⁷ Thus, even without accounting for other operating costs, or for receivables that CCC hopes to collect but may not, losses for the CCC export credit guarantee programmes outpace premiums during the period 1992-2002 by nearly \$550 million.
- Fourth, CCC's 2002 financials also report uncollectible amounts on pre-1992 CCC guarantees of \$2.567 billion.²⁰⁸ While actual data concerning premiums during the period 1981-1991 (from the first year GSM 102 was available until the last year before credit reform was introduced with the Federal Credit Reform Act) is not publicly available, Brazil has applied a proxy based on the average annual fees collected during the period 1992-2002 (\$20.24 million). Multiplying \$20.24 million by the 11 years included in the 1981-1991 period results in total fees of \$222.64 million. Thus, even without accounting for other operating costs, or for receivables that CCC hopes to collect but does not, losses for the CCC export credit guarantee programs outpace premiums during the period 1981-1991 by more than \$2.3 billion.
- Finally, the US General Accounting Office ("GAO") estimated in 1992 that if GSM 102 and GSM 103 continued until 2007, costs for the programs would reach \$7.6 billion.²⁰⁹ Premium fees

²⁰³ See Exhibit Bra-73 ("Summary of Export Credit Guarantee Programme Activity", USDA, covering GSM 102, GSM 103 and SCGP for US fiscal years 1999-2003) for the total amounts of allocations. These have been multiplied by 0.663 percent to obtain the theoretical maximum premium.

²⁰⁴ Exhibit Bra-73 ("Summary of Export Credit Guarantee Programme Activity", USDA, covering GSM 102, GSM 103 and SCGP for US fiscal years 1999-2003).

²⁰⁵ This amount is a substantial overstatement, as premiums for periods of coverage shorter than 3 years will yield substantially lower premiums of as low as 15.3 cents per \$100 as compared to 66.3 cents for a 3-year coverage. Exhibit Bra-98 ("Guarantee Fee Rate Schedule Under GSM 102 and GSM 103").

²⁰⁶ Exhibit Bra-158 (US Department of Agriculture, Office of Inspector General, Financial and IT Operations, Audit Report, *Commodity Credit Corporation's Financial Statements for Fiscal Year 2002*, Audit Report No. 06401-15-FM (December 2002), Notes to the Financial Statements, p. 14). This figure theoretically includes not only uncollectible amounts for the GSM 102, GSM 103 and SCGP programs, but also uncollectible amounts for CCC's Facility Guarantee Programme ("FGP"). Brazil has not challenged the FGP in this dispute. Brazil notes, however, that in fiscal years 1999-2003 (for which programme activity data is available on CCC's website, at <http://www.fas.usda.gov/excredits/Monthly/ecg.html>), exporter applications were only received for a total of \$4.8 million in coverage under the FGP. Thus, defaults on FGP guarantees, if any, would contribute only negligibly to the \$770 million figure discussed above.

²⁰⁷ The chart in paragraph 165 does not include premiums for 1992. Those premiums totalled \$36.14 million. See Exhibit Bra-125 (US budget for FY 1994, p. 383). According to US budget documents, premiums for the FGP are included in the budget line item for fees on the GSM and SCGP programs.

²⁰⁸ Exhibit Bra-158 (US Department of Agriculture, Office of Inspector General, Financial and IT Operations, Audit Report, *Commodity Credit Corporation's Financial Statements for Fiscal Year 2002*, Audit Report No. 06401-15-FM (December 2002), Notes to the Financial Statements, p. 14). The FGP did not exist during this period, and thus is not a factor.

²⁰⁹ Exhibit Bra-159 (US General Accounting Office, REPORT TO CONGRESSIONAL REQUESTERS, *Loan Guarantees: Export Credit Guarantee Programmes' Costs are High*, GAO/GGD-93-45 (December 1992), p.4). See also Exhibit Bra-115 (US General Accounting Office, Report to the Chairman, Subcommittee on Criminal Justice, US House of Representatives Committee on the Judiciary, "Loan Guarantees: Export Credit Guarantee Programmes' Long Run Costs are High," GAO/NSIAD-91-180, 19 April 1991, p. 2-3) ("We estimate that the

for the period 1992-2007 (assuming current rates) would only reach \$323.84,²¹⁰ demonstrating that fees for the programme do not meet costs.

In sum, CCC financials state that during the period 1981-2002, costs and losses for CCC export credit guarantee programmes exceeded premiums collected.

78. Can the United States provide supporting documentation for data used relating to "costs and losses" in paragraph 173? Could the United States confirm that the figures cited in paragraph 173 of its first written submission relate to the SCGP? Why did the United States cite these figures after stating that it is not possible to make any assessment of the long-term operating costs and losses of this programme? USA

79. In respect of what time periods does Article 13(c) require an assessment of conformity with Part V of the Agreement on Agriculture? How does this affect, if at all, your interpretation of Article 13(b)? BRA, USA

Brazil's Answer:

168. Part V of the Agreement on Agriculture requires that Members grant export subsidies in conformity with that agreement and with that Member's export subsidy reduction commitments. These commitments are made on a commodity specific basis.²¹¹ The relevant section of the US Schedule of Concessions (Part IV, Section II) clarifies that the US export subsidy commitments are to be assessed on a US fiscal year basis.²¹² A Member's export subsidy reduction commitments cover annual budgetary outlays and quantitative reduction commitments – in the US case on a fiscal year basis.²¹³ It follows that the US compliance with its export subsidy reduction commitments must be assessed on the basis of specific agricultural products and fiscal years.

169. Thus, similar to domestic support measures, the conformity of a Member's export subsidies with Part V of the Agreement on Agriculture must be assessed by comparing the amounts actually granted (both in term of budgetary outlays as well as in terms of quantities of specific agricultural products benefiting from export subsidies) with a benchmark, i.e., with a Member's export subsidy reduction commitments.

170. According to Article 33 of the Agreement on Agriculture, for agricultural products not included in Part IV, Section II of a Member's Schedule (i.e. unscheduled products) any export subsidy granted leads to a violation of Part V of the Agreement on Agriculture. Brazil's claims against Step 2 export subsidies and against ETI Act subsidies benefiting upland cotton fall in this category, as the United States does not have an export subsidy reduction commitment for upland cotton.²¹⁴ Furthermore, Brazil's claims concerning export credit guarantee programs fall in this category, in as far as export credit guarantees are available for unscheduled agricultural products.

GSM programmes will cost the Corporation about \$6.7 billion in the long run . . . This estimate assumes that the outstanding loans and guarantees remain at the same level for about 16 years and that their average risk remains unchanged as new guarantees replace old ones).

²¹⁰ This has been calculated based on actual fees for 1992-2002 and using average 1992-2002 fees as expected fees for the remainder of the time period (2003-2007).

²¹¹ See Brazil's answer to Question 7.

²¹² Exhibit Bra-83 (Schedule XX of the United States of America, Part IV, Section II entitled Export Subsidies: Budgetary Outlays and Quantitative Reduction Commitments).

²¹³ Exhibit Bra-83 (Schedule XX of the United States of America, Part IV, Section II entitled Export Subsidies: Budgetary Outlays and Quantitative Reduction Commitments).

²¹⁴ Exhibit Bra-83 (Schedule XX of the United States of America, Part IV, Section II entitled Export Subsidies: Budgetary Outlays and Quantitative Reduction Commitments).

171. For scheduled agricultural products, the Panel needs to determine whether the export subsidies for a particular scheduled agricultural product are in excess of the export subsidy reduction commitment levels for that agricultural product in the year in question, or whether the application of the export subsidies threatens to lead to circumvention of the export subsidy reduction commitments. More specifically, in this dispute, the Panel needs to assess whether the CCC export credit guarantee programmes threaten to circumvent the export subsidy reduction commitments of the United States for scheduled agricultural products.

80. In Brazil's view, why did the drafters of the Agreement on Agriculture not include export credit guarantees in Article 9.1? BRA

Brazil's Answer:

172. The negotiating history of the Agreement on Agriculture does not reveal why the drafters did not include export credits guarantees in Article 9.1, just as it does not reveal why the drafters did not include well-known and widely-used export subsidies like the United States' FSC regime in Article 9.1. Yet, the Appellate Body concluded that the FSC regime constitutes an export subsidy and is subject to the general export subsidy disciplines in the Agreement on Agriculture, including Article 10.1 thereto. As Brazil has previously noted, Article 1(e) defines export subsidies as "including" those listed in Article 9.1 of the Agreement on Agriculture, and Article 10.1 refers to a universe of export subsidies "not listed in" Article 9.1. As the Appellate Body's report in US – FSC illustrates, if a measure meets the definition of "export subsidy", it is subject to Article 10.1, even though it is not included in Article 9.1.

173. Under the Vienna Convention rules, Articles 9.1 and 10.1, as well as Article 10.2 of the Agreement on Agriculture, are to be interpreted according to their ordinary meaning, in their context, and according to the object and purpose of the Agreement on Agriculture. Brazil has demonstrated that the CCC export credit guarantee programs fulfill the definition of "export subsidy" in the Agreement on Agriculture and the SCM Agreement, and that export credit guarantees are not, under a Vienna Convention interpretation of Article 10.2, excluded from the general export subsidy disciplines in Article 10.1.

81. How does the United States respond to the following in Brazil's oral statement: USA

- (a) **paragraph 122 (rescheduled guarantees)**
- (b) **paragraph 123 (interest on debt to Treasury)**
- (c) **paragraphs 125 ff. (guaranteed loan subsidy)**
- (d) **paragraphs 127-129 (re-estimates, etc.)**
- (e) **Exhibits BRA-125-127**
- (f) **the chart on page 53 of Brazil's oral statement at the first session of the first Panel meeting relating to "Guaranteed Loan Subsidy and Administrative Expenses of US Export Credit Guarantee Programs GSM-102 GSM 103 and SCGP"?**
- (g) **In respect of (a)-(f) above, how and to what extent do the information and data presented for the export guarantee programmes concerning "program" and "financing", "summary of loan levels", "subsidy budget authority", "outlay levels", etc., in particular in Exhibits BRA-125-127, reflect "actual costs and losses" of the GSM-102, GSM-102 and SCGP export credit guarantee programmes(see e.g. Brazil's closing oral statement at the first session of the first substantive meeting, paragraph 24)? USA**

Brazil's Comment on Question 81(g):

174. Brazil may wish to comment in its rebuttal submission on the response the United States ultimately provides to this and the other sub-parts of question 81. In the meantime, however, Brazil would like to comment on the distinction between actual and estimated costs and losses.

175. As noted above in comments on Question 77, Brazil has used data from the prior year column of the US budget. This column is titled "actual," since it reflects reconciled data for a full fiscal year. Data reported in the prior year column of the "guaranteed loan subsidy" row of the US budget is "actual" in this sense. Brazil explained in paragraph 127 of its Statement at the First Panel Meeting that the FCRA calls for the CCC to make annual "reestimates" to the cost calculation and thus to the "guaranteed loan subsidy" line in the budget. Reestimates "take into account all factors that may have affected the estimate of each component of the cash flows, including prepayments, defaults, delinquencies, and recoveries,"²¹⁵ to the extent that those factors have changed since the initial estimate was made for purposes of the budget year column of the budget.

176. The results of the reestimate process are captured in the US budget and in CCC's financial statements.²¹⁶ Reestimates made in a given fiscal year are netted and recorded in the "reestimates of subsidy" (line 00.07) and "interest on reestimate" (line 00.08) lines of the US budget. In the 2002 column of the 2004 budget, for example, "reestimates of subsidy" were recorded in the amount of \$118 million, and "interest on reestimate" was recorded as \$8 million.²¹⁷ In the 2002 column of the 2004 budget, the United States in fact aggregates these two amounts with the "guaranteed loan subsidy" amount of \$97 million and the "administrative expenses" of \$4 million to arrive at a total subsidy of \$227 million (which is in turn deducted from the budgetary resources available to the CCC in line 23.95 of the budget).²¹⁸ While Brazil could have followed this same convention to accentuate the amount by which the CCC guarantee programmes' costs and losses outstrip revenue by even more than that listed in the chart included in paragraph 132 of Brazil's Statement to the First Panel Meeting, it chose to be conservative and did not do so.

177. The results of the reestimate process are also captured in a cumulative, "running tally" of the FCRA subsidy figure included in CCC's annual financial statements. CCC's fiscal year 2002 financial statements track the "credit guarantee liability" for post-1991 guarantees disbursed under the CCC export guarantee programmes. "Credit guarantee liability" is defined in the CCC financials as representing "the estimated net cash outflows (loss) of the guarantees on a net present value basis."²¹⁹ The Panel will recall that the "guaranteed loan subsidy" line in the US budget similarly tracks the net present value of payments to and from the government for CCC export guarantees, although only with respect to guarantees disbursed in one particular year. The 2002 financial statement provides a cumulative subsidy figure for all post-1991 guarantees under the CCC programmes. The analysis included in the 2002 financial statement begins with the credit guarantee liability included in the 2001

²¹⁵ Exhibit Bra-118 (Federal Accounting Standards Advisory Board, "Statement of Federal Financial Accounting Standards No. 19, Technical Amendments to Accounting Standards for Direct Loans and Loan Guarantees" in STATEMENT OF FEDERAL FINANCING ACCOUNTING STANDARDS NO. 2, March 2001, p. 15 (para. 32)). See also Exhibit Bra-160 (US Department of Agriculture, Office of the Chief Financial Officer, Credit, Travel, and Accounting Division, *Agriculture Financial Standards Manual* (May 2003), p. 80, 117, 199); Exhibit Bra-161 (US Federal Accounting Standards Advisory Board, FEDERAL FINANCIAL ACCOUNTING AND AUDITING TECHNICAL RELEASE 3, *Preparing and Auditing Direct Loan and Loan Guarantee Subsidies under the Federal Credit Reform Act* (31 July 1999), p. 17-21).

²¹⁶ According to OMB, reestimates are to be recorded in the budget. Exhibit Bra-116 (OMB Circular A-11, p. 185-4).

²¹⁷ Exhibit Bra-127 (US budget for FY 2004, p. 107).

²¹⁸ Exhibit Bra-127 (US budget for FY 2004, p. 107).

²¹⁹ Exhibit Bra-158 (US Department of Agriculture, Office of Inspector General, Financial and IT Operations, Audit Report, *Commodity Credit Corporation's Financial Statements for Fiscal Year 2002*, Audit Report No. 06401-15-FM (December 2002), Notes to the Financial Statements, p. 4).

financial statement, makes adjustments for defaults, fees and reestimates undertaken in fiscal year 2002 with respect to all post-1991 guarantees, and results in a new subsidy figure of \$411 million for those post-1991 guarantees.²²⁰ This positive net present value means that CCC has “los[t] money” during the period 1992-2002.²²¹

178. While Brazil has demonstrated that the reestimation process applied to the FCRA formula does in fact track actual data and does in fact account for actual performance of CCC export credit guarantees, Brazil notes that a certain degree of estimated data would be perfectly acceptable in an analysis of the costs and losses of guarantee programs under item (j). The purpose of the FCRA and its cost formula was, after all, “to measure more accurately the costs of Federal credit programmes,” including contingent liabilities like export credit guarantees.²²² As the United States evidently agrees, accounting for the costs of contingent liabilities like guarantees on a cash basis is not appropriate, since it masks the real costs of those guarantees. Even if the FCRA cost formula does entail the use of some estimated data, the US Congress and the President consider that that formula is the most accurate way of tracking costs.

179. Brazil notes, finally, that it is not entirely accurate to call the data used to arrive at initial estimates of the “guaranteed loan subsidy” figure “estimated” data. The US Federal Accounting Standards Advisory Board, the Government-Wide Audited Financial Statements Task Force on Credit Reform, the Office of Management and Budget and the Department of Agriculture itself have emphasized that “[m]ethods of estimating future cash flows for existing credit programs need to take account of past experience,”²²³ that “[a]ctual historical experience of the performance of a risk category is a primary factor upon which an estimation of default cost is based,”²²⁴ and that the technical assumptions underlying subsidy calculations reflect “historical cash reports and loan performance”.²²⁵ This demonstrates that “estimates” of the subsidy cost of CCC guarantees are informed by actual historical experience with borrowers.

180. Brazil also notes that a number of factors involved in setting the FCRA subsidy cost are “explicit” and not “forecast”. The Office of Management and Budget identifies contract terms such as maturity, borrower’s interest rate, fees and grace periods as “explicit,” and therefore not “estimated”.²²⁶ Moreover, as the Panel is well aware, none of the “reestimates” at issue is Brazil’s. They are all estimates by official agencies of the United States.

²²⁰ Exhibit Bra-158 (US Department of Agriculture, Office of Inspector General, Financial and IT Operations, Audit Report, *Commodity Credit Corporation’s Financial Statements for Fiscal Year 2002*, Audit Report No. 06401-15-FM (December 2002), Notes to the Financial Statements, p. 19). As noted above in Brazil’s comments on Question 77, while this figure theoretically includes CCC’s Facility Guarantee Programme (“FGP”), activity under that programme is virtually non-existent.

²²¹ Exhibit Bra-121 (US General Accounting Office (“GAO”), Report to Congressional Committees, “Credit Reform: US Needs Better Method for Estimating Cost of Foreign Loans and Guarantees,” GAO/NSIAD/GGD-95-31, December 1994, p. 20).

²²² Exhibit Bra-117 (2 U.S.C. § 661(1)).

²²³ Exhibit Bra-162 (Government-Wide Audited Financial Statements Task Force on Credit Reform, ISSUE PAPER, *Model Credit Programme methods and Documentation for Estimating Subsidy Rates and the Model Information Store*, 96-CR-7 (1 May 1996), p. 2).

²²⁴ Exhibit Bra-118 (Federal Accounting Standards Advisory Board, STATEMENT OF FEDERAL FINANCIAL ACCOUNTING STANDARDS NO. 19, *Technical Amendments to Accounting Standards for Direct Loans and Loan Guarantees in Statement of Federal Financial Accounting Standards No. 2* (March 2001), p. 16 (para. 36)). See also Exhibit Bra-160 (US Department of Agriculture, Office of the Chief Financial Officer, Credit, Travel, and Accounting Division, *Agriculture Financial Standards Manual* (May 2003), p. 120 (“In estimating default costs, the following risk factors are considered: (1) loan performance experience; . . .”).

²²⁵ Exhibit Bra-163 (Office of Management and Budget Annual Training, Introduction to Federal Credit Budgeting, 24 June 2002, p. 9).

²²⁶ Exhibit Bra-163 (Office of Management and Budget Annual Training, Introduction to Federal Credit Budgeting, 24 June 2002, p. 9).

82. Please explain each of the following statements and any possible significance it may have in respect of Brazil's claims about GSM-102 and GSM-103 (7 CFR 1493.10(a)(2), Exhibit BRA-38): BRA, USA

Brazil's Answer:

181. As discussed below, these passages corroborate evidence provided by Brazil to demonstrate that the CCC guarantee programmes constitute export subsidies within the meaning of Articles 1.1 and 3.1(a) of the SCM Agriculture, and thus within the meaning of Articles 1(e), 10.1 and 8 of the Agreement on Agriculture.

- (a) "The programmes operate in cases where credit is necessary to increase or maintain US exports to a foreign market and where US financial institutions would be unwilling to provide financing without CCC's guarantee. (7 CFR 1493.10(a)(2) Exhibit BRA-38)**

Brazil's Answer:

182. The passage cited by the Panel provides corroborating evidence that CCC guarantees provide "benefits", within the meaning of Article 1.1(b) of the SCM Agreement. Specifically, the passage states that the CCC programmes "operate in cases . . . where US financial institutions would be unwilling to provide financing without CCC's guarantee". This demonstrates at least two things. First, it establishes that the CCC guarantee programs are used in situations where, without a CCC guarantee, a borrower could not secure financing at all – not just financing on less attractive terms than could be secured with the CCC guarantee (or on terms that would constitute a benefit under Article 14(c) of the SCM Agreement), but no financing at all. Second, it establishes that financing could not be secured without a CCC guarantee – a commercial guarantee would not do. This corroborates Brazil's assertion that CCC provides something that has no equivalent on the commercial market.

183. Brazil notes that the regulations for the SCGP programme contain an identical provision, in 7 CFR 1493.400(a)(2). That section states that "[t]he SCGP operates in cases where credit is necessary to increase or maintain US exports to a foreign market and where private US exporters would be unwilling to provide financing without CCC's guarantee".²²⁷

184. Moreover, in its Annual Performance Plans for fiscal years 2000, 2001 and 2002, the US Department of Agriculture's Foreign Agricultural Service similarly stated that the SCGP programme "was created to expand high-value product exports by facilitating credit for such purchases in foreign markets lacking sufficient liquidity to purchase openly on the commercial market".²²⁸ This demonstrates that the SCGP programme extends "benefits," since it facilitates credit for the purchase of US agricultural commodities in circumstances where credit would not otherwise be available at all.

- (b) "The programmes are operated in a manner intended not to interfere with markets for cash sales. The programs are targeted toward those countries where the guarantee is necessary to secure financing of the exports but which have sufficient financial strength so that foreign exchange will be available for scheduled payments." (7 CFR 1493.10(a)(2) Exhibit BRA-38)**

²²⁷ Exhibit Bra-38 (7 CFR 1493.400 *et seq.*).

²²⁸ Exhibit Bra-164 (US Department of Agriculture, Foreign Agricultural Service, *Revised FY 2001 and FY 2002 Annual Performance Plan*, p. 11); Exhibit Bra-165 (US Department of Agriculture, Foreign Agricultural Service, *Revised FY 2000 and FY 2001 Annual Performance Plan*, p. 17).

Brazil's Answer:

185. This passage also demonstrates that CCC guarantees confer “benefits”. Specifically, the passage states that “[t]he programmes are targeted toward those countries where the guarantee is necessary to secure financing of the exports . . .”. Like the passage included in 82(a), this passage establishes at least two things. First, that without a CCC guarantee, a borrower would not be able to secure financing at all – not just financing on less attractive terms than could be secured with the CCC guarantee (or on terms that would constitute a benefit under Article 14(c) of the SCM Agreement), but no financing at all. Second, that the CCC guarantee is necessary – a commercial guarantee would not be sufficient.

186. Brazil notes that the regulations for the SCGP programme contain an identical provision, in 7 CFR 1493.400(a)(2). That section states that “The programme is operated in a manner intended not to interfere with markets for cash sales. The programme is targeted toward those countries where the guarantees are necessary to secure financing of the exports but which have sufficient financial strength so that foreign exchange will be available for scheduled payments.”²²⁹

- (c) **"In providing this credit guarantee facility, CCC seeks to expand market opportunities for US agricultural exporters and assist long-term market development for US agricultural commodities." (7 CFR 1493.10(a)(2) Exhibit BRA-38)**

Brazil's Answer:

187. This passage demonstrates that the CCC guarantee programmes are contingent on export, within the meaning of Article 3.1(a) of the SCM Agreement. Specifically, the passage establishes that the CCC guarantee programs are for use by “US agricultural exporters”. It also confirms that the programmes operate to the benefit of US exporters, who with the help of the programmes are able to expand their market share.

188. Brazil notes that the regulations for the SCGP programme contain an identical provision, in 7 CFR 1493.400(a)(2). That section states that “[i]n providing this credit guarantee facility, CCC seeks to expand market opportunities for US agricultural exporters and assist long-term market development for US agricultural commodities.”²³⁰

83. Could Brazil explain how the procedure in Annex V of the SCM Agreement would be relevant to its claims concerning agricultural export subsidies, prohibited subsidies and agricultural domestic support? (e.g. note 301 in Brazil's first submission and paragraph 4 of Brazil's oral statement at the first session of the first substantive meeting). BRA

Brazil's Answer:

189. The United States failed to respond to Brazil's questions and document requests during the Annex V procedures. Indeed, the United States refused to participate in any way in the Annex V procedures mandated by Brazil's invocation of Annex V in its request for establishment of this Panel. This refusal to participate has consequences under the express terms of Annex V. The list of Annex V questions provided to the United States by Brazil is included in Exhibit Bra-49. As directed by paragraph 6 of Annex V, given the United States' failure to cooperate in the Annex V information-gathering process, Brazil has and will present its case regarding peace clause issues and serious prejudice claims based on evidence available to it. If there are gaps in the evidence provided to the Panel by Brazil in support of its prima facie case, and those gaps are due to the United States' failure

²²⁹ Exhibit Bra-38 (7 CFR 1493.400 *et seq.*).

²³⁰ Exhibit Bra-38 (7 CFR 1493.400 *et seq.*).

to cooperate with and participate in the Annex V process, Annex V, paragraph 6 provides that “the panel may complete the record as necessary relying on best information otherwise available”.

190. As a final note, Brazil’s Annex V questions to the United States included questions concerning US agricultural export subsidies and domestic content subsidies because these are also “actionable” subsidies that cause serious prejudice to Brazil’s interests.

84. Is the Panel correct in understanding that, under the GSM-102 and GSM-103 programmes, the exporter pays a fee calculated on the dollar amount guaranteed, based on a schedule of rates applicable to different credit periods? How and on what basis are the fee rates fixed? Do the fee rates ever change? If so, how and for what reason? Would it be necessary to amend the legislation and/or regulations in order to adjust the fee rates? USA

Brazil’s Comment:

191. The Panel is correct in stating that fees for GSM 102 and GSM 103 guarantees vary only according to the dollar value of the transaction and the length of the guarantee. GSM 102 and GSM 103 fees do not otherwise vary and are charged according to a fee schedule that does not account for the country risk involved or the credit rating of the borrower. Brazil attaches news releases from the US Department of Agriculture’s Foreign Agricultural Service announcing GSM 102 and GSM 103 guarantees to Dominican Republic, Morocco, Ghana, South Korea, Vietnam and Algeria.²³¹ The Panel will note that the fees do not vary, and are based on the standard GSM 102 and GSM 103 fee schedule included as Exhibit Bra-155.²³²

192. As noted above in Brazil’s comment on Question 77, the US Department of Agriculture’s Office of the Inspector General has noted in June 2001 that “the fees CCC charges for its GSM-102 and GSM-103 export credit guarantee programmes have not been changed in 7 years and may not be reflecting current costs”.²³³ It repeated this statement in February 2002.²³⁴ Thus, GSM 102 and GSM 103 fees remained virtually unchanged from at least 1994 until February 2002. The current fee schedule demonstrates that this trend continues to the present.²³⁵

193. In reviewing the historical fee schedules available from public sources,²³⁶ Brazil notes that from at least 1994 until the present, CCC made two changes in its fee schedule for GSM 102. First, it

²³¹ Exhibit Bra-166 (US Department of Agriculture Foreign Agricultural Service, News Releases regarding extension of GSM 102 and GSM 103 guarantees to Dominican Republic, Morocco, Ghana, South Korea, Vietnam and Algeria).

²³² Exhibit Bra-155 (US Department of Agriculture Foreign Agricultural Service, *Notice to GSM-102 and GSM-103 Programme Participants*, 24 September 2002).

²³³ Exhibit Bra-153 (US Department of Agriculture Office of Inspector General Financial and IT Operations Audit Report of the Commodity Credit Corporation’s Financial Statements for Fiscal Year 2000, Audit Report No. 06401-14-FM (June 2001), p. 31).

²³⁴ Exhibit Bra-154 (US Department of Agriculture Office of Inspector General Great Plains Region Audit Report of the Commodity Credit Corporation’s Financial Statements for Fiscal Year 2001, Audit Report No. 06401-4-KC (February 2002), p. 49 (“[T]he fees CCC charged for its GSM-102 and GSM-103 export credit guarantee programmes have not been changed for many years and may not be reflecting current costs.”).

²³⁵ Exhibit Bra-155 (US Department of Agriculture Foreign Agricultural Service, *Notice to GSM-102 and GSM-103 Programme Participants*, 24 September 2002).

²³⁶ Exhibit Bra-155 (US Department of Agriculture Foreign Agricultural Service, *Notice to GSM-102 and GSM-103 Programme Participants*, 24 September 2002); Exhibit Bra-98 (US Department of Agriculture Foreign Agricultural Service, *Notice to GSM-102 and GSM-103 Programme Participants*, 4 September 2001); Exhibit Bra-156 (US Export-Import Bank, *Comparison of Major Features of Programmes Offered by Ex-Im Bank and Commodity Credit Corporation for Support of Bulk Agricultural Commodities*, available at <http://www.exim.gov/pub/ins/pdf/eib99-13.pdf>). Brazil was unable to locate from public sources other fee schedules from the period 1993-2002.

changed the fee for a 12-month guarantee with semi-annual repayment intervals from \$0.209 per \$100 of coverage to \$0.229 per \$100 of coverage. Second, it decided to offer borrowers the additional option of 30- and 60-day guarantees, at the same fee charged for 90-day and 4-, 6- and 7-month guarantees.

85. Is the Panel correct in understanding that, under the SCGP, the exporter pays a fee for the guarantee calculated on the guaranteed portion of the value of the export sales? How and on what basis are the fee rates fixed? Do the fee rates ever change? If so, how and for what reason? Would it be necessary to amend the legislation and/or regulations in order to adjust the fee rates? Please explain any "risk" assessment involved in the programme. USA

Brazil's Comment:

194. The Panel is correct in stating that fees for SCGP guarantees vary only according to the dollar value of the transaction and the length of the guarantee. SCGP fees do not otherwise vary and are charged according to a fee schedule that does not account for the country risk involved or the credit rating of the borrower. For SCGP guarantees of up to 90 days, the fee is \$0.45 per \$100 of coverage, and for SCGP guarantees from 90-180 days, the fee is \$0.90 per \$100 of coverage.²³⁷ Brazil attaches news releases from the US Department of Agriculture's Foreign Agricultural Service announcing SCGP guarantees to Tunisia, Azerbaijan, Vietnam, South Korea, Japan and Nigeria.²³⁸ The Panel will note that the fees do not vary.

86. Is there a risk categorization in relation to three export credit guarantee programmes (GSM-102, GSM-103 and SCGP)? Does this have any impact on premiums payable and the ability of the CCC to on-sell the guarantees? USA

Brazil's Comment:

195. Fees for GSM 102, GSM 103 and SCGP guarantees do not vary depending upon the credit rating of the borrower. As noted in Brazil's comments on Questions 84 and 85, guarantee fees for these three programs vary only according to the dollar value of the transaction and the length of the guarantee. Fees do not otherwise vary and are charged according to a fee schedule that does not account for the country risk involved or the credit rating of the borrower.

196. In calculating the "subsidy cost" for the purposes of the Federal Credit Reform Act, agencies like the CCC account for country risk. According to the narrative description included in the US budget,

[t]he subsidy estimates for the GSM-102 and GSM-103 programs are determined in large part by the obligor's sovereign or non-sovereign country risk grade. These grades are developed annually by the International Credit Risk Assessment System Committee (ICRAS). . . . The default estimates for GSM guarantees are determined in large part by the risk premia assigned for each risk grade.²³⁹

197. According to the GAO, "OMB requires executive branch agencies to calculate the costs of foreign loans and guarantees using annually updated ICRAS ratings and . . . country risk interest premiums when foreign loans or guarantees are budgeted, authorized, disbursed, or modified. . . ."²⁴⁰

²³⁷ Exhibit Bra-167 (12 Steps to Participating in the USDA Supplier Credit Guarantee Programme, Step 5).

²³⁸ Exhibit Bra-168 (US Department of Agriculture Foreign Agricultural Service, News Releases regarding extension of SCGP guarantees to Tunisia, Azerbaijan, Vietnam, South Korea, Japan and Nigeria).

²³⁹ Exhibit Bra-127 (US budget for FY 2004, p. 108).

²⁴⁰ Exhibit Bra-121 (GAO/NSIAD/GGD-95-31, p. 7).

198. Thus, while CCC fees for GSM 102, GSM 103 and SCGP fees do not account for country risk or the credit risk of the borrower, the “guaranteed loan subsidy” line in the US budget and the subsidy figures in the CCC’s financial statements do take account of country risk.

87. What proportion of CCC (export-related and total) long term operating costs and losses are represented by GSM-102, GSM-103 and SCGP programmes? USA

88. (a) Is the Panel correct in understanding that the United States' argument is that, at present, by virtue of Article 10.2 of the Agreement on Agriculture, there are no disciplines on agricultural export credit guarantees under the Agreement on Agriculture (or the SCM Agreement)? USA

(b) Does the United States agree with the following proposition: a WTO Member may therefore extend agricultural export credit guarantees without charging a premium, and for an indefinite period, in addition to any other terms and conditions it may wish? How would this reconcile with the title of Article 10 of the Agreement on Agriculture ("Prevention of Circumvention on Export Subsidy Commitments"), and with other commitments contained in the Agreement on Agriculture? Please cite any relevant material, including any past WTO dispute settlement cases. How would this reconcile with the United States' own statement, at paragraph 21 of its closing oral statement that "of course, the United States may not provide subsidies without any limit". USA

(c) If, as the United States argues, there are no disciplines on export credit guarantees in the Agreement on Agriculture, how could export credit guarantees "conform fully to the provisions of Part V" of the Agreement on Agriculture within the meaning of Article 13 (how can you assess "conformity" or non-conformity when there are allegedly no disciplines against which such an assessment could occur)? USA

Brazil's Comment:

199. As the Panel's question suggests, if the Panel determines that export credit guarantees are not subject to the export subsidy disciplines in the Agreement on Agriculture, the United States is nevertheless not entitled to the protection afforded by Article 13(c). Article 13(c) provides an exemption from action for those export subsidies that “conform fully to the provisions of Part V” of the Agriculture Agreement. If, as the United States argues, export credit guarantees are not subject to Part V, then they cannot “conform fully to the provisions of Part V,” and are not entitled to the safe haven in Article 13(c).

200. The panel in *Canada – Aircraft* (21.5) took a similar approach with respect to the safe haven included in the second paragraph of item (k) to the Illustrative List of Export Subsidies appended to the SCM Agreement.²⁴¹ The second paragraph of item (k) provides as follows:

Provided, however, that if a Member is a party to an international undertaking on official export credits to which at least twelve original Members to this Agreement are parties as of 1 January 1979 (or a successor undertaking which has been adopted by those original Members), or if in practice a Member applies the interest rates provisions of the relevant undertaking, an export credit practice which is in conformity with those provisions shall not be considered an export subsidy prohibited by this Agreement.

²⁴¹ Panel Report, *Canada – Aircraft* (21.5), para. 5.143-5.145.

The “international undertaking on official export credits” cited in this provision is the Organization for Economic Co-operation and Development’s Arrangement on Guidelines for Officially Supported Export Credits (“OECD Arrangement”).²⁴²

201. To determine whether a particular Canadian measure could benefit from the safe haven in the second paragraph of item (k), the Panel first reviewed which types of “export credit practices” could potentially be “in conformity with” the “interest rates provisions” of the OECD Arrangement. According to the Panel, it could only “determine the conformity of a given export credit practice with those interest rate provisions . . . [if] it is of the type that conceptually could be subject to, and thus in conformity with, those provisions”.²⁴³ Similarly, if the United States is correct that CCC export credit guarantees are not subject to the disciplines in Part V of the Agriculture Agreement, then CCC guarantees cannot logically “conform fully to the provisions of Part V” and trigger the exemption from action provided for in Article 13(c).

- (d) **Is the United States advocating the view that its own export credit guarantee programmes, which pre-dated the Uruguay Round, are effectively "grandfathered" so as to benefit from some sort of exemption from the export subsidy disciplines of the Agreement on Agriculture? How, if at all, is it relevant that the SCGP did not, according to the United States, become relevant for upland cotton until the late 1990's (i.e. after the entry into force of the WTO Agreement)? USA**

F. STEP 2 PAYMENTS

89. Does the United States confirm Brazil's statement in paragraph 331 of its first submission that "The conditions and requirements for Step 2 domestic payments remain unchanged with the passage of the 2002 FSRI Act"? What is the relevance of this, if any, to this dispute? USA

90. Does the United States confirm Brazil's statement in paragraph 235 of its first submission that the changes concerning Step 2 export payments from the 1996 FAIR Act to the 2002 FSRI Act are: increase in the amount of the subsidy by 1.25 cents per pound and the removal of any budgetary limits that applied under the 1996 FAIR Act? What is the relevance of this, if any, to this dispute? USA

91. What is the significance of the elimination of the 1.25 cent threshold payment in the 2002 FSRI Act pertaining to Step 2 payments? USA

92. Does the United States confirm that Exhibit BRA-65 represents a sample contract for exporters of eligible upland cotton to conclude with the CCC under the FSRI 2002, and that an application form (Exhibit BRA-66) needs to be filled out with data on weekly exports and submitted to the USDA FAS. Is Exhibit BRA-66 - Form CCC 1045-2 – also a valid example? If not, please identify any differences or distinctions. USA

²⁴² Available at <http://www.oecd.org/dataoecd/52/3/2763846.pdf>.

²⁴³ WT/DS70/RW, para. 5.93. The Panel concluded that “the only forms of export credit practices” subject to the interest rate provisions of the *OECD Arrangement* are “direct credits/financing, refinancing and interest rate support,” since only those forms of official financing support are subject to the *Arrangement*’s commercial interest reference rates (“CIRR”) – “the only *existing* systems of minimum interest rates under the *Arrangement*.” *Id.*, paras. 5.98, 5.101 (emphasis in original). Since the CIRR are only expressed as fixed rates, the Panel concluded that they could only be applied to fixed (and not floating) interest rate transactions. *Id.*, para. 5.102. Nor could the CIRR be applied to official support with a shorter maturity than two years (the minimum term expressly listed in the *OECD Arrangement*), or to guarantees or insurance. *Id.*, para. 5.106.

Brazil's Comment:

202. Brazil includes a new version of the current "Upland Cotton Domestic User/Exporter Agreement" (Revision 7, in effect as of 1 August 2003 and issued on 17 June 2003), which replaces Revision 6 that Brazil has included as Exhibit Bra-65 to its First Submission.

93. Please elaborate why the United States deems that Step 2 payments upon submission of proof of export are not subsidies contingent upon export. Is it the US contention that, in order to be contingent on export, exportation must be the exclusive condition for receipt of the payment? USA

94. Is the Panel correct in understanding that Brazil alleges an inconsistency with Article 3.1(b) of the SCM Agreement only with respect to Step 2 domestic payments? BRA

Brazil's Answer:

203. Yes.

95. Do the criteria in 7 CFR 1427.103(c)(2) (Exhibit BRA-37) that Step 2 "eligible upland cotton" must be "not imported cotton" apply to both domestic and export payments? USA

96. Is a domestic sale a "use" for the purposes of Step 2 payments? Is a sale for export, or export, considered a "use"? USA

97. How does the United States respond to Brazil's assertion, at paragraph 70 of Brazil's oral statement at the first session of the first substantive meeting, that "It is obvious that a single bale of cotton cannot be both exported and used domestically." Is this a relevant consideration? USA

98. How many Step 2 payments are received if a bale of upland cotton is exported, and then opened by a domestic user in the United States, or vice versa? USA

99. How does the United States respond to Brazil's arguments in paragraphs 71-75 of Brazil's oral statement at the first session of the first Panel meeting concerning the relevance of the Appellate Body Report in US-FSC (21.5). USA

100. How does Brazil respond to the statement in note 119 of the United States' first written submission that "...to the extent a consumer that had intended to export instead opens the bale, then that consumer could still obtain the Step 2 payment upon submission of the requisite documentation". The Panel notes that Step 2 payments all involve upland cotton produced in the United States. What are the two distinct factual situations that Step 2 payments involve? Other than the panel report in Canada-Dairy and the findings of the Appellate Body in US-FSC (21.5)²⁴⁴, do any other dispute settlement reports offer guidance on this issue? For example, how, if at all is the Appellate Body's report in Canada-Aircraft relevant here?²⁴⁵ BRA

²⁴⁴ "We recall that the ETI measure grants a tax exemption in two different sets of circumstances: (a) where property is produced *within* the United States and held for use *outside* the United States; and (b) where property is produced *outside* the United States and held for use *outside* the United States. Our conclusion that the ETI measure grants subsidies that are export contingent in the first set of circumstances is not affected by the fact that the subsidy can also be obtained in the second set of circumstances. The fact that the subsidies granted in the second set of circumstances *might* not be export contingent does not dissolve the export contingency arising in the first set of circumstances.²⁴⁴ Conversely, the export contingency arising in these circumstances has no bearing on whether there is an export contingent subsidy in the second set of circumstances. Where a United States taxpayer is simultaneously producing property within and outside the United States, for direct use

Brazil's Answer:

204. The applicable regulations (7 CFR 1427.104)²⁴⁶ define eligible domestic users and exporters of upland cotton.²⁴⁷ To receive a Step 2 export payment, a person (including a cotton producer or a cooperative) must be "regularly engaged in selling eligible [US] upland cotton for export".²⁴⁸ To receive a domestic payment, a person must be "regularly engaged in the business of opening bales of eligible [US] upland cotton to manufacture US upland cotton into cotton products in the United States".²⁴⁹ The only actor who can be indifferent whether they export or use cotton domestically is a hypothetical domestic US cotton product manufacturer regularly engaged in opening US bales for domestic US manufacture that also regularly engages in exporting US cotton. In that situation, if a bale of cotton is opened by mistake instead of being exported, the exporter who is also the US cotton product manufacturer will receive a Step 2 domestic payment for that bale if the company has already entered into a contract with CCC for Step 2 payments, and subject to proof that bale is in fact used for manufacturing cotton products in the United States. But even if that hypothetical situation were to occur, then the payment would be contingent upon the domestic use of only US upland cotton (prohibited by Article 3.1(b) of the SCM Agreement). And if the bale were exported, the US exporter would receive the Step 2 payments subject to proof of export of US (not foreign) upland cotton (prohibited by Article 3.1(a) of the SCM Agreement).

205. It follows that the "two distinct factual situations" resulting in the payment of Step 2 subsidies are (1) the domestic "use" of eligible US upland cotton by a manufacturer of cotton products regularly engaged in opening bales; and (2) the "export" of eligible US cotton by exporters regularly engaged in selling US upland cotton. The United States argues that this case is distinguishable from US – FSC (21.5) because in that case one situation involved property produced within the United States and held for use outside the United States, and the other situation involved property produced outside the United States and held for use outside the United States.²⁵⁰ This is irrelevant.

206. The point of the distinction by the Appellate Body in US – FSC (21.5) was not the geographic location of the property at issue, but rather whether one portion of payment under a programme was export contingent. In fact, in US – FSC (21.5), the products found to be subject to the export contingency were those produced within the United States and held for use outside the United States. This is exactly the situation with Step 2 export payments. Upland cotton produced in the United States receives Step 2 payment upon proof of export ("held for use outside the United States") outside the United States. As in US – FSC (21.5), the fact that subsidies available under the programme are also granted in a second situation, i.e., when upland cotton produced within the United States is used within the United States "does not dissolve the export contingency arising in the first set of circumstances".²⁵¹

outside the United States, subsidies may be granted under the ETI measure in respect of both sets of property. The subsidy granted with respect to the property produced within the United States, and exported from there, is export contingent within the meaning of Article 3.1(a) of the *SCM Agreement*, irrespective of whether the subsidy given in respect of property produced outside the United States is also export contingent."

²⁴⁵ There, the Appellate Body stated that,

"the fact that some of TPC's contributions, in some industry sectors, are *not* contingent upon export performance, does not necessarily mean that the same is true for all of TPC's contributions. It is enough to show that one or some of TPC's contributions do constitute subsidies "contingent ... in fact ... upon export performance".

²⁴⁶ Exhibit Bra-37 (7 CFR 1427.104).

²⁴⁷ First Submission of Brazil, paras 92, 98.

²⁴⁸ Exhibit Bra-37 (7 CFR 1427.104(a)(2)).

²⁴⁹ Exhibit Bra-37 (7 CFR 1427.104(a)(1)).

²⁵⁰ First Oral Statement of the United States, paras. 21-22.

²⁵¹ Appellate Body Report, *US – FSC (21.5)*, para. 119.

207. Concerning other relevant dispute settlement reports, Brazil believes that the Canada – Aircraft decision is useful precedent. In that case, Canada argued that Technology Partnership Canada (TPC) was a funding mechanism providing “support to a broad base of sectors and technologies” “that result in a high technology product or process for sale in domestic and export markets”.²⁵² Canada claimed that “Brazil has not adduced any evidence to show that TPC contributions are contingent on export performance, in the sense that the contributions would not be paid unless exports took place, that there would be rewards if exports took place. . .”.²⁵³ The Appellate Body affirmed the panel’s finding of export contingency, noting that “it is enough to show that one or some of TPC’s contributions do constitute subsidies ‘contingent . . . in fact . . . upon export performance.’”²⁵⁴ This finding is consistent with the Appellate Body’s later decision in US – FSC (21.5). It stands for the proposition that where a programme makes some payments contingent upon export of products, the fact that other payments under the programme are made for domestic use does not eliminate the export contingency of the programmes.

101. How does Brazil respond to the United States' assertion at paragraph 22 of its oral statement that the programme involves "eligible users" who constitute the "entire universe" of potential purchasers of upland cotton? BRA

Brazil’s Answer:

208. Brazil considers that the United States’ statement is not correct. As noted in the previous answer, an “eligible” user cannot include firms that are not “regularly engaged in” opening bales of upland cotton for manufacturing upland cotton products in the United States or exporting upland cotton from the United States.²⁵⁵ The eligible domestic user criteria exclude all firms that are domestic cotton brokers or simple resellers. Nor would “eligible domestic users” include firms that have not entered into CCC contracts or who open bales but do not use them in the manufacture of upland cotton products or who only occasionally open bales of upland cotton for manufacture of upland cotton products. Similarly, the regulations for eligible “exporters” do not include persons who occasionally export and who are, thus, not considered to be persons “regularly engaged” in exporting upland cotton.²⁵⁶ Furthermore, the regulations do not cover exporters who have not entered into a CCC contract as exporters eligible for payment.²⁵⁷

102. How does Brazil respond to the United States' assertion at paragraph 129 of its first written submission, that "[t]he programme is indifferent to whether recipients of the benefit of this programme are exporters or parties that open bales for the processing of manufacturing raw cotton into cotton products in the United States." BRA

Brazil’s Answer:

209. Brazil notes that the same “programme indifference” argument could have been made by the United States in the US – FSC (21.5) case (tax deferred whether products produced within or outside the United States) or by Canada in the Canada – Aircraft case (TPC payments made whether products consumed or used domestically or exported). These two Appellate Body decisions clarify that what matters is whether one segment of the programme is contingent upon export. This is consistent with the Article 3.1(a) text that the export contingency be “solely or as one of several other conditions”. Step 2 export payments are clearly contingent upon proof of export of US upland cotton by eligible exporters. The fact that another class of persons in a different situation (domestic users) also may

²⁵² WT/DS70/R, paras. 6.231, 6.235

²⁵³ WT/DS70/R, para. 6.248.

²⁵⁴ *Canada – Aircraft*, WT/DS70/AB/R, para. 179.

²⁵⁵ Exhibit Bra-37 (7 CFR 1427.104(a)(1)).

²⁵⁶ Exhibit Bra-37 (7 CFR 1427.104(a)(2) and (b)).

²⁵⁷ Exhibit Bra-37 (7 CFR 1427.104(a)(2) and (b)).

receive the payment does not remove this export contingency. Additionally, Brazil notes that Step 2 domestic payments violate Article 3.1(b).

103. Is the Step 2 programme fund a unified fund that is available for either domestic users or exporters, without a specific amount earmarked for either domestic users or exporters? Please substantiate your response, including by reference to any applicable statutory or regulatory provisions. USA

104. How does the United States respond to the data presented in Exhibit BRA-69? Is it accurate? Please substantiate. USA

105. Why is the Step 2 programme separated into "domestic users" and "exporters"? Apart from differentiating between exporters and domestic users, with consequential differentiation as to the forms that must be filled out and certain other conditions that must be fulfilled, are the eligibility criteria for Step 2 payments identical? Are the form and rate of payment, as well as the actual payment made, identical? USA

106. With respect to paragraph 139 of the United States' first written submission, are Step 2 export payments included in the annual reduction commitments of the United States? If so, why? USA

107. Please comment on any relevance, to Brazil's de jure claims of inconsistency with the provisions of the Agreement on Agriculture, of Exhibit BRA-69, which shows Step 2 payments made to (i) domestic users and (ii) exporters. This Exhibit shows that, from FY 91/92 through 02, the Step 2 payments for exporters exceeded those for domestic users in FY 94; FY 95; FY 96 (in fact there were no domestic payments in FY 96); and FY 02. In the other years, the domestic payments are greater than export payments. BRA, USA

Brazil's Answer:

210. This document is not relevant for either Brazil's Article 3.1(a) or Article 3.1(b) claims under the SCM Agreement. Even if the Step 2 export payments were zero in certain years (which they have never been), it would not remove the export contingency. Similarly, the fact that Step 2 domestic payments were not made in one time period does not resolve their contingency upon use of domestic over imported upland cotton. Brazil's claims are that whenever a Step 2 payment for exported or domestically used upland cotton takes place, this payment is required to be made in a manner inconsistent with Articles 3.1(a) or 3.1(b) of the SCM Agreement and with Articles 3.3 and 8 of the Agreement on Agriculture in the case of Step 2 export payments.

108. At paragraph 135 of its first written submission, the United States states : "[T]he subsidy is not contingent upon export performance..." (emphasis added). Again, in the course of the first Panel meeting, the United States admitted that the Step 2 payments were "subsidies". Does the United States thus concede that Step 2 payments constitute a "subsidy" within the meaning of the WTO Agreement? USA

109. How does the United States respond to Brazil's arguments concerning a mandatory/discretionary distinction and the allegation that certain United States measures (including s.1207(a) of the 2002 FSRI Act) are mandatory? (This is referred to, for example, in paragraph 28 of Brazil's first written submission). Does the United States agree with the assertion that (subject to the availability of funds) the payment by the Secretary of Step 2 payments is mandatory under section 1207(a) FSRI upon fulfilment by a domestic user or exporter of the conditions set out in the legislation and regulations? If not, then why not? To what extent is this relevant here? What determines the "availability of funds"? Please cite any

other relevant measures or provisions which you consider should guide the Panel in respect of this issue. USA

110. Section 1207(a) of the 2002 FSRI Act provides that during the period beginning on the date of the enactment of the FSRI Act through July 31 2008, " .. the Secretary shall issue marketing certificates or cash payments, at the option of the recipient, to domestic users and exporters for documented purchases by domestic users and sales for export by exporters...". The Panel notes that Brazil does not appear to distinguish between the treatment of (i) cash payments and (ii) marketing certificates in terms of the issue of whether or not a "subsidy" exists. The United States refers to "benefits" and "payments" and "program" in asserting that Step 2 is not export contingent (paragraphs 127-135 of the United States' first written submission).

- (a) Do the parties thus agree that there is no need to draw any distinction between the treatment of (i) cash payments and (ii) marketing certificates in terms of the issue of whether or not a "subsidy" exists for the purposes of the Agreement on Agriculture? BRA, USA

Brazil's Answer:

211. Brazil agrees there is no need to draw any distinction between cash payments and "commodity certificates". The Step 2 regulations indicate that Step 2 payments "shall be made available in the form of commodity certificates issued under part 1401 of this Chapter, or in cash, at the option of the programme participants".²⁵⁸ Part 1401 of the regulations indicated that commodity certificates may be exchanged for cash.²⁵⁹

- (b) Why would a domestic user or an exporter select to receive a marketing certificate over a cash payment? What is the proportion of cash payments vs. marketing certificates granted under the programme? USA

111. Does the United States maintain its argument that actions based on Article 3.1(b) of the SCM Agreement are conditionally "exempt from actions" due to the operation of Article 13 of the Agreement on Agriculture? USA

112. In the event that the Panel finds that Article 6.3 of the Agreement on Agriculture does not preclude an examination of Brazil's claims under Article 3.1 of the SCM Agreement and Article III:4 of GATT 1994, how does the United States respond to the merits of Brazil's claims relating to Step 2 payments under those provisions? USA

113. Is it necessary for measures directed at agricultural processors included in AMS to discriminate on the basis of the origin of goods? USA

114. With respect to the last sentence of paragraph 22 of Brazil's closing oral statement, could Brazil elaborate on the circumstances in which a local content subsidy would comply with Article 3.1(b) of the SCM Agreement? BRA

Brazil's Answer:

212. Brazil believes the Panel is referring to paragraph 21 of the final "as delivered" version of Brazil's Closing Statement on 24 July 2003. The text of this sentence reads as follows: "There is also no conflict between Article 3.1(b) of the SCM Agreement and Agriculture Agreement Article 6 or

²⁵⁸ Exhibit Bra-37 (7 CFR 1427.106).

1. ²⁵⁹ Exhibit Bra-34 (7 CFR 1401.4(a)).

Annex 3, paragraph 7, because there are two types of domestic subsidies – those that comply with Article 3.1(b) of the SCM Agreement and those that do not.” Paragraph 85 of Brazil’s First Oral Statement of 22 July 2003 was more precise in focusing on the relevant type of support, i.e., support provided to processors of agricultural products, stating that “[t]here are two types of ‘non-green box’ support to processors that could benefit producers of agricultural goods: support that violates ASCM Article 3.1(b) and GATT Article III:4 and support that does not.”

213. There are no circumstances in which a “local content subsidy” would comply with Article 3.1(b) of the SCM Agreement.

115. What is the meaning and relevance (if any) to Brazil's claims under Article 3 of the SCM Agreement and Article III:4 of GATT 1994 of the phrase "measures directed at agricultural processors shall be included to the extent that such measures benefit the producers of the basic agricultural products" in the Agreement on Agriculture? BRA, USA

Brazil's Answer:

214. The phrase from Annex 3, paragraph 7 of the Agriculture Agreement cited by the Panel requires Members to tabulate and include as part of AMS to individual products an amount of benefit provided to producers of basic agricultural products resulting from “measures directed at agricultural processors. . .”. The obligations of Members to comply with reduction commitments tied to AMS, and the obligations of Members under SCM Article 3 and GATT Article III, all apply cumulatively and simultaneously. This phrase recognizes that subsidies to processors of agricultural products may benefit producers of the basic agricultural product and, thus, must be included within total AMS. However, as Brazil has argued, this phrase does not provide an exemption from the SCM Agreement or GATT Article III for such subsidies, and no such exemption can be interpolated into the text.²⁶⁰ The cumulative nature of the obligations incurred under the WTO Agreement results in the prohibition of certain “measures directed at agricultural processors” that otherwise would be included in the AMS calculation, namely those that are contingent upon the use of domestic over imported agricultural products contrary to Article 3.1(b) of the SCM Agreement.

116. With respect to paragraph 32 of the oral statement of the EC, are subsidies contingent on the use of domestic goods consistent with the Agreement on Agriculture? Does the phrase "provide support in favour of domestic producers" in Article 3.2 of the Agreement on Agriculture refer to, and/or permit such subsidies? BRA, USA

Brazil's Answer:

215. Brazil agrees with the EC that Articles 1(a), 3.2, 6.3 of the Agreement on Agriculture include the phrase “domestic support in favour of agricultural producers”. And Brazil further recognizes that all types of “domestic support in favour of agricultural producers” must be tabulated for the purposes of setting and enforcing a Member’s domestic support reduction commitments (Total AMS). But Brazil notes that neither the EC nor the United States can point to any inherent conflict between these provisions and the prohibition of local content subsidies under Article 3.1(b) of the SCM Agreement for the reasons set forth in Brazil’s First Oral Statement and in Brazil’s answer to the Panel’s Question 114.²⁶¹

216. The EC and the United States fail to acknowledge that there can be subsidies/domestic support measures provided to processors of the basic agricultural product that can be consistent with Article 3.1(b) of the SCM Agreement and that also “provide support in favour of domestic producers”. The EC appears to assume that all support to processors of a basic agricultural

²⁶⁰ First Oral Statement of Brazil, paras. 81-86.

²⁶¹ First Oral Statement of Brazil, paras. 81-86.

commodity violates Article 3.1(b) of the SCM Agreement. That is simply not correct. Yet, without this assumption, there is no inherent conflict between the SCM Agreement and the Agreement on Agriculture. The absence of any conflict coupled with the absence of any explicit exemption for local content subsidies in Article 13(b) or anywhere else in the Agreement on Agriculture supports the conclusion that local content subsidies related to agricultural goods violate Article 3.1(b) of the SCM Agreement.

117. What is the relationship between Step 2 payments to exporters and the marketing loan payments, both of which appear to compensate for the price differences relative to the Liverpool A-Index? For example, is there double compensation? Or is one of the explanations that these export-related price compensatory payments are paid to different operators (namely, the producer, on the one hand under the marketing loan arrangements, and the processor/users (Step 2 programme) arrangements on the other? USA

118. Can the United States confirm that it does not rely on Article III:8 of GATT 1994? USA

G. ETI ACT

119. How does the United States respond to Brazil's reference to the panel report in India - Patents (EC) (at paragraph 138 of its oral statement at the first session of the first substantive meeting)?²⁶² How, if at all, should the Panel take this report into account in considering the issues raised by Brazil's claims relating to the ETI Act? USA

120. Concerning its claims on the ETI Act, Brazil relies on the US – FSC case. However, it appears that the United States did not raise the issue of the Peace Clause in that case, nor did the United States appear to invoke Article 6 of the Agreement on Agriculture. If the Panel's understanding is correct, how, if at all, are these differences relevant here? Could you direct the Panel to any relevant findings or conclusions by the panel or Appellate Body in that case? BRA

Brazil's Answer:

217. Brazil is not aware that there are any differences between the US position regarding the peace clause in the US – FSC case and the present case. There is no reference in the entire record of that dispute that the United States ever asserted that the EC's claims regarding the ETI Act were exempt by the peace clause. Also in this dispute, Brazil is not aware that the United States has ever asserted that Brazil's claims regarding the ETI Act were exempted by the peace clause. In this regard, the United States has taken a consistent approach in the present case and in US – FSC.

218. Because the United States never raised the peace clause as a defense in US – FSC, there were no findings by the panel or the Appellate Body regarding the peace clause. And neither the panel nor the Appellate Body held that the EC was required to demonstrate that the United States was not entitled to peace clause protection before proceeding to the substance of the EC's claims against the ETI Act. In any event, the United States has been unable to establish that the ETI Act is consistent

²⁶² That panel stated: "It can thus be concluded that panels are not *bound* by previous decisions of panels or the Appellate Body even if the subject-matter is the same. In examining dispute WT/DS79 we are not legally bound by the conclusions of the Panel in dispute WT/DS50 as modified by the Appellate Body report. However, in the course of "normal dispute settlement procedures" required under Article 10.4 of the *DSU*, we will take into account the conclusions and reasoning in the Panel and Appellate Body reports in WT/DS50. Moreover, in our examination, we believe that we should give significant weight to both Article 3.2 of the *DSU*, which stresses the role of the WTO dispute settlement system in providing security and predictability to the multilateral trading system, and to the need to avoid inconsistent rulings (which concern has been referred to by both parties). In our view, these considerations form the basis of the requirement of the referral to the "original panel" wherever possible under Article 10.4 of the *DSU*." (footnote omitted)

with Part V of the Agreement on Agriculture. Therefore, the United States does not enjoy peace clause exemption under Article 13(c) of the Agreement on Agriculture.

121. How do you respond to the reference in paragraph 43 of EC third party oral statement with respect to the relevance of Article 17.14 of the DSU, and, in particular, the phrase "a final resolution to that dispute" (emphasis added)? Please explain the use, and relevance (if any) of the term "disputes" in Articles 9.3 and 12 and Appendix 3 of the DSU, and please cite any other provisions you consider relevant. USA, BRA

Brazil's Answer:

219. Brazil is of the view that DSU Article 17.14 requires that following the adoption of an Appellate Body report, the parties to the dispute, i.e., the defending and complaining Member, are unconditionally bound by the results of that report. This interpretation is consistent with the Appellate Body decisions in *US – Shrimps (21.5)*²⁶³ and *EC – Bed Linen (21.5)*,²⁶⁴ both confirming that panel and Appellate Body reports adopted by the Dispute Settlement Body must be considered final resolutions to a dispute between the parties to that dispute. There is no precedent in the WTO or GATT that would require the Panel to find that the United States alone is bound in this case. It is difficult to imagine, however, how the United States could take a different position in defending against Brazil's ETI claims in this case, in light of the adoption by the DSB of the Appellate Body and panel reports in *US – FSC (21.5)*, and the recommendation by the DSB that the United States bring the ETI Act into conformity with the Agreement on Agriculture and the SCM Agreement.

220. In this case, Brazil challenges exactly the same measure as that found by the panel and the Appellate Body in *US – FSC (21.5)* to violate the Agreement on Agriculture and the SCM Agreement. There have been no changes to the ETI Act since the adoption of the panel and Appellate Body reports by the WTO Dispute Settlement Body.²⁶⁵ Brazil challenges the ETI Act with exactly the same rationale as the EC. Thus, there is a complete identity between the "measure" and the "claims" in this case and the *US – FSC (21.5)* dispute (noting that upland cotton is a sub-set of all the products covered by the ETI Act). Under these circumstances, it is appropriate for the Panel to make similar findings of fact, conclusions of law, and recommendations as the panel and Appellate Body in *US – FSC (21.5)*.²⁶⁶

221. Brazil does not consider any of the other provisions cited by the Panel to be relevant to this particular question. Should the Panel wish Brazil to elaborate on any of provisions more specifically, Brazil will be pleased to do so.

²⁶³ Appellate Body Report, *US – Shrimps (21.5)*, para. 97.

²⁶⁴ Appellate Body Report, *EC – Bed Linen (21.5)*, para. 90-96.

²⁶⁵ The United States has indicated in its First Submission (para. 189) that both branches of Congress are considering legislative proposals that would repeal the ETI Act. However, Brazil notes that it has been over 18 months since 29 January 2002, the date on which the panel and Appellate Body reports on the ETI Act were adopted by the DSB.

²⁶⁶ First Oral Statement of Brazil, paras. 138-39.

ANNEX I-2

ANSWERS OF THE UNITED STATES TO THE QUESTIONS FROM THE PANEL TO THE PARTIES FOLLOWING THE FIRST SESSION OF THE FIRST SUBSTANTIVE PANEL MEETING

(11 August 2003)

UPLAND COTTON

1. Please confirm that all information and data that you have provided to the Panel relating to "cotton" in fact relates to upland cotton only. BRA, USA

1. The United States can confirm that, with the exception of export credit guarantees, all of the information and data we have provided to-date relates to upland cotton only. With respect to export credit guarantees, the Commodity Credit Corporation does not maintain data to distinguish transactions involving different types of cotton (for example, upland cotton versus extra-long staple (ELS) cotton). However, the United States has no reason to believe that types of cotton other than upland cotton constitute a material percentage of such transactions.

PRELIMINARY ISSUES

Product scope of Panel's terms of reference relating to Brazil's export credit guarantee claims

3. If the request for consultations in this dispute omitted certain products in relation to export credit guarantees, on what basis is it argued that it failed to identify the measures at issue in accordance with Article 4.4 of the DSU? USA

2. The only export credit guarantee measures identified in the Brazilian consultation request were those in respect of upland cotton. The request for consultations did not identify export credit guarantee measures for any other agricultural commodities.

3. The request for consultations identified the measures subject to consultations in a single sentence:¹

The measures that are the subject of this request are prohibited and actionable subsidies provided to US producers, users and/or exporters of upland cotton¹, as well as legislation, regulations, statutory instruments and amendments thereto providing such subsidies (including export credits), grants, and any other assistance to the US producers, users and exporters of upland cotton ("US upland cotton industry").

¹ Except with respect to export credit guarantee programmes as explained below.

Another sentence followed this one, setting out (in a page and a half) a listing of measures that were included within the identification in the first sentence.

4. Apart from the footnote, the first two lines of the sentence quoted in the previous paragraph address "subsidies provided to US producers, users and/or exporters of upland cotton"; thus, apart

¹WT/DS267/1, at 1.

from the footnote, it is clear that subsidies provided to US producers of, say, soybeans are not included within the scope of the request. Equally, apart from the footnote, it is clear that subsidies provided to, say, banks that finance US cotton exports (but do not produce, use or export cotton) are not included within the scope of the request. To give an example from another part of the request, Brazil's consultation request identified "[e]xport subsidies provided to exporters of US upland cotton under the FSC Repeal and Extraterritorial Income Exclusion Act of 2000" as a challenged measure. Having identified that measure at issue for purposes of DSU Article 4.4 as subsidies provided to upland cotton exporters under that legislation, Brazil could not then have included in its panel request such subsidies provided to exporters of all agricultural commodities or all industrial goods.

5. Brazil, however, contends that "[t]he footnote clarifies that Brazil's request with respect to export credit guarantees is *not* limited to upland cotton."² Brazil's contention is incorrect. The footnote does nothing more than direct the reader of the consultation request to look "below" for an explanation. The footnote by itself does not contain any "identification of [a] measure at issue" as required by DSU Article 4.4, and therefore cannot itself bring any additional measures within the scope of the consultation request. Any such additional measures would have to be found -- if anywhere -- in an explanation "below."

6. However, as described in the first US submission, no such explanation or identification of additional measures ever appears. In fact, though Brazil devoted several paragraphs to this issue in its oral statement, it has never pointed to any explanation of any kind -- or any other identification of additional measures -- "below."

7. In addition, the statement of evidence attached to Brazil's consultation request did not include any evidence related to measures other than those for upland cotton. For Brazil to now argue that its consultation request was broader than its statement of evidence is for Brazil to admit that its consultation request was in breach of Article 7.2 of the Subsidies Agreement. Brazil cannot have it both ways.³

8. In summary, while Brazil's consultation request did identify measures at issue for purposes of DSU Article 4.4, the measures it actually identified did not include export credit guarantees for agricultural commodities other than cotton. Thus, the latter measures were not within the scope of consultations, were not consulted upon, and could not have been included in Brazil's panel request.

4. Is it argued that the export credit guarantee programmes concerning upland cotton are each a separate or independent measure, in that they operate independently? USA

9. The CCC export credit guarantee programme (GSM-102), the CCC intermediate export credit guarantee programme (GSM-103), and the Supplier Credit Guarantee Programme (SCGP) each constitute separate programmes. The distinct operation of the programmes themselves is manifested in both the terms of the particular programmes as well as in the nature of the obligation guaranteed. The GSM-102 and GSM-103 programmes guarantee obligations of banks. SCGP extends exclusively to obligations of importers. Obligations guaranteed under the GSM-102 programme may not extend beyond three years. SCGP guarantees a far lower percentage of principal (65 per cent).

10. Within each programme, allocations are made by country, by commodity, and by amount.⁴ Thus, discrete programming decisions are made in connection with each such country, commodity,

²Brazil's Opening Oral Statement, para. 90.

³In light of the Panel's intended finding on the scope of Brazil's consultation request with respect to export credit guarantees, the United States will be making a request for a preliminary ruling on this point.

⁴See 7 C.F.R. §§ 1493.4, 1493.5 (setting forth allocation criteria). These criteria also apply to SCGP. 7 C.F.R. § 1493.400.

programme, and amounts (in terms of a guarantee value).⁵ As a result, for the last 10 fiscal years, for example, as described in the First Written Submission of the United States, no cotton transactions occurred under the GSM-103 programme.

11. Furthermore, each export credit guarantee issued is a separate measure. Under DSU Article 4.4, it is incumbent upon Brazil to identify in its consultation request “the measures at issue.” Here, Brazil identified the measure as “export credit guarantees . . . to facilitate the export of US upland cotton,” and the United States may, and did, rely on that consultation request (including the attached statement of evidence) for notice.

5. Is there a specification in any legislation or regulation (or any other official government document) which limit or restrict the export credit guarantee programmes at issue exclusively to upland cotton? USA

12. Programme announcements issued pursuant to applicable programme regulations (7 C.F.R. §§ 1493.10(d), 1493.400(d)) serve to limit the availability of CCC export credit guarantees. These limitations are expressed in terms of one or more of the following criteria: commodities, total guarantee value for individual commodities, destination, and time within which export must occur. Examples of such programme announcements are included as Exhibit US-12. Thus, export credit guarantee offerings through programme announcements may be limited to cotton, pursuant to the authority of programme regulations.

6. For the purposes of the Panel's examination of Brazil's claims relating to GSM-102, GSM-103 and SCGP under the Agreement on Agriculture and the SCM Agreement, is accurate data and information available with respect to these export credit guarantee programmes concerning upland cotton alone (e.g. with respect to "long-term operating costs and losses")? In this respect, the Panel also directs the parties' attention to the specific questions below relating to the programmes. USA

13. The United States endeavoured to provide precisely such data with respect to cotton alone in paragraph 173, and associated tables, in its First Written Submission.

7. Are commitments with respect to export subsidies under the Agreement on Agriculture commodity-specific? How, if at all, is this relevant? BRA, USA

14. Export subsidy commitments under the Agriculture Agreement are, indeed, commodity specific. Each Member may have a schedule of reduction commitments with respect to specified commodities. To illustrate, the export subsidy reduction commitment schedule of the United States is attached as Exhibit US-13. As reflected in that schedule, for each of the 12 scheduled commodities, the United States has a reduction commitment with respect to both budget outlays and subsidized quantities. Other Members have similar schedules involving different commodities and reduction commitments. In all cases, however, the budgetary and quantitative commitments are unique to each commodity on each Member’s respective schedule of export subsidy reduction commitments.

15. An individual Member, therefore, could apply an export subsidy programme with respect to all commodities for which it has undertaken reduction commitments. By operation of such an export subsidy programme, however, a Member may be in conformity with none, some, or all of its commodity-specific reduction commitments. So long as a Member applies such export programme in a given year in accordance with the commodity-specific reduction commitment for each year, such export subsidy programme is permitted with respect to each commodity and conforms fully with respect to Part V of the Agreement on Agriculture. The fact that commitments are taken on a product-

⁵See Exhibit US-12.

specific basis confirms that alleged export subsidy measures can be defined on a product-specific basis – and that is exactly what Brazil did here.

16. In contrast, for those specific commodities for which such Member does not have a reduction commitment, then such Member may not provide export subsidies at all in connection with such specific commodities. As a result, the same programme that, as applied, may be entirely in conformity with that Member's reduction commitment vis-à-vis one commodity may be a prohibited subsidy with respect to another commodity.

8. Does the United States confirm that the questions referred to by Brazil in paragraph 92 of Brazil's oral statement were posed to the United States in the consultations? USA

17. Yes. When Brazil posed them during the consultations, the United States immediately objected to questions about commodities other than cotton as being outside the scope of the consultations (as paragraph 94 of Brazil's oral statement acknowledges).

9. How does the United States respond to paragraph 94 of Brazil's oral statement? USA

18. It is incumbent on the complaining party to identify the specific measure at issue, and it should not fall to the responding party to intuit that measures not specified in the request for consultations are considered included by the complaining party. This deprives the responding party of an opportunity to understand the measures that are at issue and to enjoy the benefit of appropriate consultations. In the final analysis, Brazil essentially argues that its consultation questions and statement at consultations could expand the scope of the measures at issue as identified in its consultation request beyond "export credit guarantees . . . to facilitate the export of US upland cotton." This is not the case. (For further information, please refer to the US answer to Question 3.)

10. What actual prejudice, if any, has the United States suffered as a result of the alleged omission of products other than upland cotton from the request for consultations? USA

19. The issue of prejudice is not relevant to the question of whether a measure not consulted upon may be the subject of panel proceedings. The requirement of consultations at the beginning of a dispute is a central characteristic of the dispute settlement system, and is reflected throughout DSU Article 4. Consultations serve a number of important functions, including helping the parties to understand each others' concerns and aiding in efforts to resolve the dispute. The DSU affirms the importance of consultations and *requires* that a Member cannot proceed to a panel unless the Member has consulted on that measure.

20. Article 4.4 delimits the scope of the consultations through its requirement that the complaining Member identify the measures at issue. In light of the jurisdictional nature of the consultation requirement, Article 4.4's explicit requirement that the measures be identified serves the useful role of establishing a bright line as to the matters which are within the scope of the consultations and the dispute. Any resort to an analysis of what topics were actually discussed at the consultations – beyond conflicting with the DSU Article 4.6 requirement that consultations "shall be confidential," designed to facilitate the resolution of the dispute – would invite litigation over the unverifiable recollections of each party.

21. The United States notes that in past disputes in which the scope of the dispute was at issue, it was accepted as a given that the consultation request defined the scope of the consultations. For example, in the *US – Import Measures* dispute, the European Communities did not assert that US actions taken on 19 April 1999 were the subject of consultations even though consultations took place two days later, on 21 April 1999. Instead, accepting that its 4 March 1999, consultation request delimited the scope of the consultations, and could not have covered measures taken after that time,

the EC argued (unsuccessfully) that the April 19 actions were the same measure as that identified in the 4 March consultation request.⁶

22. Brazil's consultation request identified export credit guarantees on upland cotton as the sole export credit guarantee measures within the scope of the consultations and, hence, the dispute. Had it wished to include export credit guarantees with respect to other products within the scope of the consultations, Brazil could have re-filed its consultation request to include these guarantees, much as other Members have re-filed consultation requests when they have wished to expand the scope of the dispute.⁷ Brazil chose not to, instead apparently hoping to be relieved of the procedural requirements of the DSU, requirements enforced with respect to, and taken seriously by, other Members.⁸

23. While prejudice is not relevant to whether the scope of this dispute includes export credit guarantees for products other than upland cotton, the United States observes that, not only *has* it suffered prejudice as a result of Brazil's omission of allegations concerning products other than upland cotton, but more importantly, the United States *will* suffer even further prejudice if it is compelled to respond to allegations that Brazil never properly included in its request for consultations. The United States has suffered an inability to prepare, respond, and consult with respect to allegations on measures never presented to the United States in accordance with the DSU. The United States was entitled to rely on the measures identified by Brazil in its request for consultations and also rely on that which Brazil declined to put at issue by its failure to so state in its request. This justifiable reliance is furthered by Brazil's failure to amend its request for consultations after ample notice from the United States of its reasonable understanding of Brazil's request.

24. Consequently, the US has not had proper opportunity to consult with respect to the application of the three separate export credit guarantee programmes and their specific application to the myriad of commodities exported in connection with these programmes nor with respect to the conformity of the WTO obligations of the United States with the application of such programmes to such commodities. If export credit guarantees with respect to other eligible commodities were now included in this dispute, the United States will suffer the prejudice of having to prepare and defend its actions in a severely compressed time frame without the benefit of any consultations whatsoever.

11. Does the United States agree that Brazil's request for establishment of the Panel can be understood to indicate that Brazil's export credit guarantee claims relates to products other than upland cotton? How, if at all, is this relevant? USA

25. Brazil's panel request changed the language relating to export credit guarantees to include the words "other eligible agricultural commodities." However, Brazil may not unilaterally alter the scope of the "measures at issue" in its panel request simply by adding measures not previously identified. Thus, while Brazil would have been free to add additional *claims* in its panel request, it was not free to broaden the scope of the challenged *measures*.

26. Indeed, Brazil and at least one third party have argued that in two SPS disputes between the United States and Japan panels found that a complaining party may introduce new claims in its panel

⁶ Appellate Body report, *United States - Import Measures on Certain Products of the European Communities*, WT/DS165/AB/R, adopted 10 January 2001, para.70.

⁷ See, e.g., WT/DS204/1 & WT/DS204/1/Add.1 (consultation request supplemented to add measures); WT/DS174/1 & WT/DS174/1/Add.1 (consultation request to add consultations under additional covered agreement).

⁸ The United States refers the Panel to the preliminary ruling of the panel in the *Canada Wheat Board* dispute, WT/DS276/12, which necessitated the re-filing of the US panel request and establishment of a second panel. Likewise, the United States refers the panel to India's re-filing of its panel request in the *US Rules of Origin* dispute (WT/DS243/5/Rev.1) when made aware of deficiencies in that request at the DSB meeting at which the request was considered. See also WT/DS210/2 & WT/DS210/2/Rev.1.

request that were not included in its consultation request. In both of these cases, Japan argued that the United States could not introduce new claims (cite to new legal provisions) not in its consultation request. The United States argued, and both panels agreed, that every legal claim need not be included in the consultation request. However, these disputes are not relevant here because they did not involve identifying a new *measure* in the panel request. As noted in the 3d party oral statement of Benin, “claims” and “measures” are distinct concepts; indeed, the distinction between “claims” and “measures” is fundamental.⁹

12. Please address issues and submit evidence regarding the three export credit guarantee programmes concerned relating to upland cotton and other eligible agricultural commodities in your answers to questions and rebuttal submissions. BRA, USA

27. In light of the Panel's preliminary ruling and without prejudice to the US position that these measures are not within the scope of this dispute, the United States will respond to Brazil's arguments in the US submissions.

13. Please include any argumentation and evidence to support your statement during the Panel meeting that the inclusion of such other eligible agricultural commodities would create additional "work" for the Panel with respect to each of these commodities under Article 13 of the Agreement on Agriculture. USA

28. Article 10.2 defers disciplines on, *inter alia*, export credit guarantees until such time as internationally agreed disciplines are reached – as Members hope to do in the Doha Development Round. Therefore, export credit guarantees are not export subsidies within the meaning of the Agriculture Agreement, and Article 13(c) does not apply. However, for purposes of argument, we note that Article 13(c)(ii) of the Agreement on Agriculture provides that:

(c) export subsidies that conform fully to the provisions of Part V of this Agreement, as reflected in each Member's schedule, shall be:

* * * * *

(ii) exempt from actions based on Article XVI of GATT 1994 or Articles 3, 5, and 6 of the Subsidies Agreement.

Pursuant to Article 13(c)(ii), to the extent a Member *is* providing export subsidies in conformity with its reduction commitments under Part V of the Agreement on Agriculture, such export subsidies are exempt from action under Article XVI of the GATT and Articles 3, 5, and 6 of the SCM Agreement.

29. Article 13(c) is not relevant with respect to export subsidies granted in connection with commodities not subject to reduction commitments in the applicable schedule of the Member. For example, the United States does not have a reduction commitment with respect to upland cotton. Therefore, the United States may not provide any export subsidy for upland cotton. The Peace Clause protection of Article 13(c) therefore cannot apply to any theoretical export subsidy of the United States for upland cotton.

30. In contrast, however, the United States has reduction commitments for 12 commodities. (Please refer to the response of the United States to Question 7 for a description of how the export subsidy reduction commitments – and therefore export subsidy obligations – of the United States and all other members are, therefore, commodity specific.) Because such commitments are commodity specific, the extent to which Article 13(c)(ii) may apply to export subsidy measures of the United

⁹See, e.g., Appellate Body Report, *Guatemala – Anti-Dumping Investigation Regarding Portland Cement from Mexico*, WT/DS60/AB/R, adopted 25 November 1998, para. 72.

States is also commodity specific. Conformity with WTO obligations and the application of Article 13(c)(ii) to export credit guarantees with respect to those twelve commodities could only be evaluated by an examination of *each* commodity subject to reduction commitments.

Expired measures

14. Please submit evidence regarding the programmes under the 1996 FAIR Act, in particular, production flexibility contract payments and market loss assistance payments, to the extent that they would be relevant to the Panel's determination under Article 13 of the Agreement on Agriculture in your answers to questions and rebuttal submission. USA

31. The United States will present evidence and arguments regarding payments under the 1996 Act as may be relevant to the Panel's Peace Clause analysis with respect to those measures.

15. Do the parties agree that it is beyond a Panel's power to recommend a remedy for an expired measure? Could the Panel be required to examine "expired measures" in order to conduct its assessment of the matter before it? How, if at all, is Article 7.8 of the SCM Agreement relevant to these matters? BRA, USA

32. The United States agrees that it is beyond a panel's power to recommend that a Member bring into conformity a measure that no longer exists.¹⁰ However, more fundamentally, the issue is whether the expired measures in this dispute could have been measures affecting the operation of any covered agreement within the meaning of DSU Article 4.2 or "measures at issue" within the meaning of DSU Article 6.2. Because the production flexibility contract payments and market loss assistance payments were completed, the programmes terminated, and the statutory instruments providing them superseded before Brazil's consultation and/or panel requests were filed, they could not have been "measures at issue," and they could not properly have been consulted upon or brought within the terms of reference of the Panel. This is a broader concern than whether the Panel may recommend a remedy since findings cannot be made with respect to such expired measures.

33. To determine whether past subsidies may currently be challenged, it is useful to distinguish between recurring and non-recurring subsidies. A non-recurring subsidy is a measure that continues in existence for the duration of the allocation of the subsidy to production.¹¹ For example, a subsidy to acquire capital stock to be used in future production would be non-recurring and allocated over the useful life of the stock. Where a subsidy is non-recurring and is allocated to future production¹², the measure (subsidy) may continue to be actionable even if the authorizing programme or legislation has expired. For example, in the *Indonesia – Autos* dispute, where a non-recurring subsidy was provided, the panel deemed the measure to continue even though the subsidy programme had allegedly been terminated (and it is worth noting that the termination allegedly occurred well after the panel and consultation requests– in fact, after the second panel meeting).

34. In contrast, a recurring subsidy is typically provided year-after-year and is made in respect of current rather than future production. Once production has occurred and the measure been replaced or

¹⁰Appellate Body Report, *United States – Import Measures on Certain Products from the European Communities*, WT/DS165/AB/R, adopted 10 January 2001, para. 81.

¹¹*See, e.g.*, Report by the Informal Group of Experts to the Committee on Subsidies and Countervailing Measures, G/SCM/W/415, para. 12 (25 July 1997) ("Whether a subsidy is oriented towards production in future periods, consists of equity, or is carried forward in the recipient's accounts were viewed as related to the question whether its benefits persist beyond a single period, and hence whether it should be allocated to future periods.").

¹²Subsidies Agreement, Annex IV, para. 7 (referring to "[s]ubsidies . . . the benefits of which are allocated to future production").

superseded, there would no longer be any measure in existence to challenge. Accordingly, a Report by the Informal Group of Experts to the Committee on Subsidies and Countervailing Measures suggested that recurring subsidies – such as grants for purposes other than the purchase of fixed assets and price support payments – should be expensed, or attributed to a single year, rather than allocated over some multi-year period.¹³

35. In the case of production flexibility contract payments and market loss assistance payments, these measures were subsidies allocated to a particular crop or fiscal year by the respective authorizing legislation. Pursuant to the 1996 Act, the last production flexibility contract payment was made for fiscal year 2002 (1 October 2001 – 30 September 2002) “not later than” 30 September 2002.¹⁴ Pursuant to legislation enacted on 13 August 2001, the last market loss assistance payment was for the 2001 marketing year (1 August 2001 – 31 July 2002), that is, for market conditions prevailing in that year.¹⁵ Once the relevant fiscal year and marketing year, respectively, had been completed, these measures would no longer exist. Thus, by the time of Brazil’s consultation and/or panel requests, there were no measures to consult upon nor to be at issue under the DSU; production flexibility contracts and market loss assistance payments therefore do not fall within the Panel’s terms of reference.

Agricultural Assistance Act of 2003

16. What, if any, prejudice in terms of the presentation of its case does the United States allege, should the Panel proceed to consider the measures constituting the cottonseed payments under the Agricultural Assistance Act of 2003? USA

36. It has been a fundamental characteristic of both the GATT 1947 and the WTO dispute settlement systems that proposed measures may not be the subject of dispute settlement. This has meant that dispute settlement proceedings, including consultations, could not begin until the measure at issue actually came into existence. In seeking to bring into the scope of this dispute the Agricultural Assistance Act of 2003, Brazil is seeking to fundamentally expand and change the nature of WTO dispute settlement. This issue goes well beyond the question of whether a particular responding party is prejudiced in a particular dispute and cannot be resolved on the basis of whether such prejudice has occurred. The reasons that the United States would be prejudiced if the Panel considered any measure under the Agricultural Assistance Act of 2003, including a cottonseed payment under that Act, are the reasons that the dispute settlement system has been organized to only allow proceedings on actual, not proposed, measures. First, the responding party would have lost the benefit of consultations on these measures. Consultations serve a number of important functions, including helping the parties to understand each others’ concerns and aiding in efforts to resolve the dispute. The DSU affirms the importance of consultations and *requires* that a Member cannot proceed to a panel unless the Member has consulted on that measure. Likewise, the DSU requires that the “measures at issue” be identified in the panel request, and non-existent measures quite simply are not measures at all.

37. Apart from reflecting the importance Members have placed on consultations, the DSU’s requirement that a measure exist before it can be the subject of dispute settlement proceedings avoids a waste of resources since anticipated measures may never come into effect, or may, when enacted, be in substantially changed form. Further, allowing challenges to measures not yet in existence would

¹³G/SCM/W/415, paras. 1-12; *id.*, Recommendation 1, at 26-27.

¹⁴Federal Agriculture Improvement and Reform Act of 1996, § 112(d)(1), Public Law No. 104-127 (4 April 1996); 7 US Code § 7212(d)(1).

¹⁵Public Law No. 107-25, § 1(a) (23 Aug. 2001) (“The Secretary of Agriculture ... shall, to the maximum extent practicable, use \$4,622,240,000 of funds of the Commodity Credit Corporation to make a market loss assistance payment to owners and producers on a farm that are eligible for a final payment for fiscal year 2001 under a production flexibility contract for the farm under the Agriculture Market Transition Act.”).

effectively authorize panels to issue advisory opinions. Should Members desire to expand the scope of the dispute settlement system in this manner, they may do so – indeed could only do so – through amendment of the DSU. The DSU now requires the existence of a measure before consultations may be requested or a panel established.

38. Finally, were the issue of the specific prejudice to the United States relevant in deciding whether a panel's terms of reference could include a measure not in existence at the time of consultations or the panel request, the United States notes that this dispute is already complex, with multiple measures at issue involving multiple claims. To require the United States to address Brazil's allegations on the Agricultural Assistance Act of 2003 would detract from the time and resources available to respond to questions and make arguments relating to those measures that *are* properly within the terms of reference.

17. (a) **What is the relationship of the Agricultural Assistance Act of 2003 to other legislation in the request for establishment of the Panel? BRA, USA**
- (b) **Do the legal instruments follow directly one after another, or are there temporal gaps? Are payments authorized under a broad legislative authority or are they specific to each legal instrument? BRA, USA**
- (c) **Please provide any implementing regulations. Do these implementing regulations resemble those relating to previous programmes or payments? Are payments made retrospectively? How if at all is this relevant? BRA, USA**

39. (a) The Agricultural Assistance Act of 2003¹⁶ was part of a large piece of legislation covering a diverse range of topics. The Act had several disaster provisions including some relief for sugar interests and more generalized relief for persons who lost other crops. One of the provisions provided for a cottonseed payment to be applied to the 2002 cotton crop (the crop that was harvested in that calendar year):

Sec. 206. COTTONSEED. The Secretary shall use \$50,000,000 of funds of the Commodity Credit Corporation to provide assistance to producers and first-handlers of the 2002 crop of cottonseed.

No law compelled or authorized the cottonseed payment for the 2002 crop except for the 2003 Act, which bears no relation to other legislation cited by Brazil.

40. There was no cottonseed payment authorized in either 2002 or 2001 for the 2001 crop. Cottonseed payments were made for the 1999 and 2000 crops. Of the three pieces of legislation authorizing cottonseed payments for the 1999 and 2000 crops, only one arguably may be found in Brazil's consultation and panel requests. Brazil identifies the "Crop Year 2001 Agricultural Economic Assistance Act (August 2001)" as a challenged measure. The Emergency Agricultural Assistance Act, Public Law No. 107-25 (13 August 2001), authorized a cottonseed payment of \$85 million. In addition, Section 204(e) of Public Law No. 106-224, enacted 20 June 2000, directed the Secretary to use \$100 million of Commodity Credit Corporation (CCC) funds to provide assistance to producers and first handlers of the 2000 crop of cottonseed. Finally, the cottonseed payment for the 1999 crop was authorized by section 104(a) of Public Law No. 106-113, enacted 19 Nov. 1999; \$79 million in residual funds were used for the 1999 crop programme.

41. (b) The temporal gaps between the various cottonseed payments are indicated in the answer to (a), above. That is, no cottonseed payments were made in 2001 or 2002 for the 2001 crop (nor

¹⁶Public Law No. 108-7 (Feb. 23, 2003).

prior to 1999). This gap serves to emphasize that these payments are *ad hoc*, and there was no legislative guarantee that there would be a payment for any of the years involved until the payment was actually authorized. Thus, what Brazil has termed the "cottonseed programme" is readily distinguished from those programmes under the 2002 Act that recur for each crop harvested from 2002 through 2007.¹⁷ In contrast, the legal authority for each cottonseed payment was separate and distinct; no underlying piece of legislation mandated that cottonseed payments be made.

42. (c) We note that each time a cottonseed payment is authorized, new rules must be issued to disburse the funds because there is no ongoing cottonseed "programme"; thus, when new rules are issued, the old rules are either removed at the same time or had been removed previously. That is, there is no publication that included rules for all three programmes.

43. The cottonseed payment under the 2003 Agricultural Assistance Act is not related to the other cottonseed payments except by subject matter. As indicated at the panel hearing, the text in the Agricultural Assistance Act (quoted above) is broad and simple, leaving much to the Department of Agriculture. Because of the discretion vested in the Secretary to disburse the 2002 crop cottonseed payment, and for reasons of administrative convenience, the 2003 regulations borrow from the regulations that implemented the cottonseed payments for the 2000 crop and for the 1999 crop. On 25 April 2003, the Department published regulations at 68 Federal Register 20331 to disburse funds in respect of the 2002 crop.¹⁸ The regulations to disburse the 2000 crop cottonseed payment were published at 65 Federal Register 65718 (2 November 2000).¹⁹ The regulations to disburse the 1999 crop cottonseed payment were published on 8 June 2000 at 65 Federal Register 36550.²⁰

ARTICLE 13(B): DOMESTIC SUPPORT MEASURES

"exempt from actions"

20. **In paragraph 8 of its initial brief (dated 5 June, 2003), the United States argued that the word "actions" as used in the phrase "exempt from actions" in Article 13 of the Agreement on Agriculture includes the "bringing of a case" and consultations. In paragraph 36 of its first written submission (dated 11 July, 2003), the United States stated as follows:**

"[P]rior to this point in the process, the DSU rules did not afford the United States any opportunity to prevent the dispute from proceeding through consultations and panel establishment automatically, regardless of the US insistence that its measures conform to the Peace Clause."

Is it the United States' understanding that the drafters used the phrase "exempt from actions" knowing that under the DSU it would not be possible fully to exempt "actions", as the United States interprets that term? USA

44. There is a difference between a commitment to exempt from action and the mechanism to enforce that commitment, just as there is a difference between rights and obligations under the WTO and the mechanism to enforce those rights and obligations. For example, where one Member

¹⁷Farm Bills are initiated by Agricultural Committees of the US Congress and recur every 5 or 6 years. Programmes provided for in a Farm Bill are generally not tied to finite amounts of money but rather make use of the funds of the Commodity Credit Corporation (CCC), which has borrowing authority in the US Treasury. *See* 15 US Code § 713 a-11 *et seq.* As a result, no appropriation is needed. By contrast, cottonseed payments (similar to other disaster payments) are *ad hoc* with targeted monies.

¹⁸Exhibit US-14.

¹⁹Exhibit US-15.

²⁰Exhibit US-16.

breaches a tariff binding, another Member will need to resort to dispute settlement in order to resolve the issue. This does not mean that it is not possible to fully obligate the Member to observe its tariff bindings. The similar situation arises with respect to procedural obligations as well.

45. When responding Members have been confronted by situations in which they considered that complaining parties did not meet requirements for invoking dispute settlement procedures, those responding Members can voice their objections at consultations and the DSB meetings at which panel establishment has been considered, but then must accept that the issue will ultimately be decided by the panel. For example, notwithstanding that the DSU requires consultations on a measure before a panel may be established, there is no mechanism available to address a complaining party's failure to consult absent resolution by a panel.

46. Responding Members have allowed jurisdictional issues to go to the panel for resolution as a practical way forward that offers sufficient protection for their interests while also protecting the integrity of the dispute settlement system. This does not mean that responding Members in any way lost their rights, for example, to consult on the measures at issue before being subject to panel proceedings; it has simply been practical to allow the issue to be decided by panels.

47. Likewise, in this dispute, the fact that Brazil has attempted improperly to invoke dispute settlement procedures notwithstanding the Peace Clause – and the fact that the United States has accepted that the issue should be resolved by the Panel – does not and cannot diminish the right of the United States to be exempt from Brazil's action. The fact that Members may disregard their obligations, or act based on a misunderstanding of the facts or obligations, does not affect those obligations. In this case, Brazil considers that the Peace Clause is inapplicable. As our argumentation to date indicates, we disagree and consider that, based on a correct reading of the law and facts, the Peace Clause is applicable, and Brazil was obliged not to bring this dispute. Upon making a finding on this issue in our favour, the Panel would effectively be concluding that Brazil's invocation of dispute settlement was improper – even if undertaken in good faith – just as panels have in the past concluded that complaining parties have improperly included measures that were not consulted upon in their panel requests or claims that were not within the panel's terms of reference in their argumentation.

21. In US - FSC and US - FSC (21.5) the Appellate Body made findings under the SCM Agreement relating to export subsidies in respect of agricultural products without making a finding in respect of Article 13 of the Agreement on Agriculture. How is this relevant to the United States' interpretation of the phrase "exempt from actions" as used in Article 13? USA

48. The FSC findings are not relevant since they do not address the Peace Clause issue. The issue was not raised by either party, and so neither the panel nor the Appellate Body made any finding with respect to Article 13, nor did they offer any reasoning on this issue. Indeed, in the absence of any party raising or arguing this issue, it would be difficult to see how the panel or Appellate Body could have made any findings concerning Article 13. Those DSB recommendations and rulings thus provide no guidance for purposes of this dispute.

"such measures" and Annex 2 of the Agreement on Agriculture

22. Please explain the difference, if any, between the meaning of "defined" and the meaning of "fixed" in the phrase "a defined and fixed base period" in paragraph 6(a) of Annex 2 of the Agreement on Agriculture. BRA, USA

49. These terms should be interpreted according to the customary rules of interpretation of public international law. The ordinary meaning of "defined" is "clearly marked, definite" and "set out

precisely.”²¹ “Fixed” means “stationary or unchanging in relative position.”²² Thus, as used in paragraph 6(a), a “defined and fixed base period” means a base period that is “set out precisely” and “stationary or unchanging in relative position.” That is, the “definite” base period must not be “changing in relative position”; for example, the “base period” for purposes of determining “base acres” for the deficiency payments under the 1990 Act was a farm’s average acreage over the three most recent years²³, and so, was not a “fixed” base period but a moving one. On the other hand, US direct payments satisfy this criterion because eligibility is determined by historical production of any of a number of crops (including upland cotton) in a base period that is “definite” (set out in the 2002 Act) and “stationary or unchanging in a relative position” (does not change in relative position for the duration of the 2002 Act).

23. Please explain the meaning of "a" in "a defined and fixed base period" in paragraph 6(a) of Annex 2 of the Agreement on Agriculture, the meaning of "the" in "the base period" in paragraphs 6(b), (c) and (d), and the difference between these and the phrase "based on the years 1986-88" in Annex 3. BRA, USA

50. Paragraph 6(a) establishes that eligibility for payments under a decoupled income support measure shall be determined by clearly-defined criteria in “a defined and fixed base period.” That is, paragraph 6(a) does not mandate that any particular base period be used for a decoupled income support measure and does not mandate that the same base period be used for all decoupled income support measures. This contrasts with the use of the phrase “the base period” in paragraph 9 of Annex 3, which is defined in that same paragraph as “the years 1986 to 1988.”²⁴

51. Paragraphs 6(b), (c), and (d) use the term “the base period.” As these subparagraphs all follow paragraph 6(a), in which eligibility is set in “a” defined and fixed base period, the later references to “the base period” should be read to refer to the base period used for eligibility under paragraph 6(a). Again, because paragraph 6(a) does not mandate that any particular base period be used (as opposed to paragraph 9 of Annex 3), “the base period” for paragraphs 6(b), (c), and (d) will be the “defined and fixed base period” used for purposes of eligibility under the decoupled income support measure. The definite article “the” is commonly used to refer back to a member of a indefinite set identified by the indefinite article “a.” For example, it would be common grammatically to say: “A Member may take action if the Member makes the appropriate notification to the WTO.”

24. How often can a Member define and fix a base period in accordance with paragraph 6 of Annex 2 of the Agreement on Agriculture? BRA, USA

52. Paragraph 6 establishes policy-specific criteria applying to a decoupled income support measure. Under paragraph 6(a), eligibility for payments under such a measure shall be determined by criteria “in a defined and fixed base period.” Other policy-specific criteria under paragraph 6 establish that the amount of payments under a decoupled income support measure shall not be related to or based on the type or volume of production, the prices, or the factors of production employed in any year after the base period used for purposes of determining eligibility under paragraph 6(a).

²¹*The New Shorter Oxford English Dictionary*, vol. 1, at 618 (1993 ed.).

²²*The New Shorter Oxford English Dictionary*, vol. 1, at 962 (1993 ed.).

²³See US First Written Submission, para. 101 n. 92.

²⁴Agriculture Agreement, Annex 3, paragraph 9 (“The fixed external reference price *shall be based on the years 1986 to 1988* and shall generally be the average f.o.b. unit value for the basic agricultural product concerned in a net exporting country and the average c.i.f. unit value for the basic agricultural product concerned in a net importing country *in the base period.*”) (emphasis added). See also *id.*, Annex 3, paragraph 5 (“The AMS calculated as outlined below for *the base period* shall constitute the base level for the implementation of the reduction commitment on domestic support.”) (emphasis added). Appellate Body Report, *Korea - Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WT/DS161/AB/R - WT/DS169/AB/R, adopted 10 January 2001, paras. 115-16.

Thus, with respect to a decoupled income support measure, the base period used must be “defined and fixed.”

53. There is no requirement in paragraph 6 that a *particular* base period be used for a decoupled income support measure nor that the *same* base period be used for purposes of every decoupled income support measure. Thus, so long as the base period for a particular measure is “defined and fixed,” this element of the policy-specific criteria in paragraph 6 will be met.

54. For purposes of this dispute, the base period for US direct payments under the 2002 Act is defined by the 2002 Act and fixed for the duration of the 2002 Act – that is, for marketing years 2002-2007. Thus, one “defined and fixed base period” applies for payments under the US direct payment programme for the six-year period to which the 2002 Act applies.

25. Does the United States consider that there is any ambiguity in the term "type of production" as used in paragraph 6(b) of Annex 2 of the Agreement on Agriculture? USA

55. When read according to the customary rules of interpretation of public international law, the United States does not consider that the meaning of the term “type . . . of production” as used in paragraph 6(b) is ambiguous or obscure. This paragraph establishes that the amount of decoupled income support payments may not be “based on, or linked to, the type or volume of production . . . undertaken in any year after the base period.” Interpreted according to the ordinary meaning of the terms, in context, and in light of the object and purpose of the Agriculture Agreement, this provision means that a decoupled income support measure may not base or link payments to production requirements, whether by type or volume.

26. Can the United States confirm Brazil's assertions in paragraph 174 of its first written submission that the implementing regulations for direct payments prohibit or limit payments if base acreage is used for the production of certain crops? If so, can the United States clarify the statement in paragraph 56 of its first written submission that direct payments are made regardless of what is currently produced on those acres? Can the United States confirm the same point in relation to production flexibility contracts? USA

56. The 2002 Act allows any commodity or crop to be planted on base acres on a farm for which direct payments are made with limitations regarding certain commodities. Those commodities are fruits, vegetables (other than lentils, mung beans, and dry peas), and wild rice. Planting of those commodities on base acres is prohibited, except: (1) in a region with a history of double-cropping those commodities with those crops the historical production of which makes acres eligible for direct payments, double-cropping is permitted; (2) on a farm with a history of planting those commodities, planting is permitted, and direct payments would be reduced for every acre so planted; and (3) for a producer with a history of planting those commodities, planting is permitted, and direct payments would be reduced for every acre so planted.²⁵

57. To be more precise, the third sentence of paragraph 56 of the US first submission should have used the phrase “whether upland cotton” in place of “what.” As the United States has previously indicated,²⁶ direct payments are not “related to, or based on, the type or volume” of current production

²⁵Farm Security and Rural Investment Act of 2002, § 1106 (“2002 Act”) (Ex. US-1).

²⁶US First Submission, para. 22 (“These [direct] payments are made with respect to farm acreage that was devoted to agricultural production in the past; the payments, however, are made regardless of whether upland cotton is currently produced on those acres or whether anything is produced at all.”); *id.*, para. 24 (“As stated, no current production of upland cotton (or any other crop) is required to receive payment – or, put another way, the payment is the same regardless of how much, or any, upland cotton is produced.”); *id.*, para. 67 (“Not only is there no requirement that a direct payment recipient engage in any particular type or volume of

because there is *no requirement* that a recipient produce upland cotton or any other crop in order to receive these payments. Direct payments are made with respect to farm acreage that was devoted to agricultural production in the past. In its rebuttal submission, the United States will describe production flexibility contract payments, which would share these characteristics but not others with direct payments, and explain why production flexibility contract payments are “green box” measures.

29. Please explain the meaning of the words “the fundamental requirement” as used in paragraph 1 of Annex 2 of the Agreement on Agriculture. USA

58. “Fundamental” means “[s]erving as the base or foundation” and “primary, original; from which others are derived.”²⁷ A “requirement” is “[s]omething called for or demanded.”²⁸ Thus, the “fundamental requirement” that measures for which exemption from reduction commitments under Article 6 is claimed must have “no, or at most minimal, trade-distorting effects or effects on production” is “something called for or demanded” “from which others are derived.”

59. The United States, perhaps in distinction from the European Communities, does not view this “requirement” (“something called for or demanded”) as merely setting out in hortatory terms the objective of Annex 2. However, as suggested by the use of the word “fundamental” (“from which others are derived”) and the structure of Annex 2 (that is, beginning the second sentence with the word “accordingly”), compliance with the fundamental requirement of the first sentence will be demonstrated by conforming to the basic criteria of the second sentence plus the applicable policy-specific criteria of paragraph 6 through 13. Relevant context supports this interpretation: Articles 6.1, 7.1, and 7.2 refer to measures which are not subject to reduction commitments because they qualify under “*the criteria* set out in Annex 2.” Article 18.3 requires a Member to notify “details of the new or modified measure and its conformity with the *agreed criteria* as set out either in Article 6 or in Annex 2.” Annex 2 itself, in describing the policy-specific criteria that must be met under paragraphs 2 and 5, emphasizes that measures must meet the “*basic criteria* set out in paragraph 1” rather than the “fundamental requirement” of that paragraph.

60. The text and context of paragraph 1 is also confirmed by the object and purpose of the Agriculture Agreement. Members need to be able to design green box measures with certainty that these measures will be exempt from reduction commitments so that they can meet their binding commitments on domestic support in furtherance of the goal of “substantial progressive reductions in agricultural support . . . sustained over an agreed period of time.”²⁹ Assessing the conformity of a claimed green box measure against the “fundamental requirement” of the first sentence in isolation would be a difficult, if not impossible task, for a Panel. Members foresaw the problem and therefore provided guidance on how a measure would fulfill that fundamental requirement – that is, if the measures “conform to the . . . basic criteria” of the second sentence plus any applicable policy-specific criteria, they shall be deemed to have met the fundamental requirement of the first sentence of Annex 2.

30. Do the parties consider that direct payments and production flexibility contract payments meet or met the basic criteria referred to in paragraph 1 of Annex 2 of the Agreement on Agriculture? BRA, USA

61. The “basic criteria” referred to in paragraph 1 of Annex 2 are: (a) the support in question shall be provided through a publicly-funded government programme (including government revenue

production, a recipient need not engage in any current agricultural production in order to receive the direct payment.”); US Opening Statement at the First Panel Meeting, para. 18 (“The payments, however, are made regardless of whether cotton is currently produced on those acres or whether anything is produced at all.”).

²⁷*The New Shorter Oxford English Dictionary*, vol. 1, at 1042 (1993 ed.)

²⁸*The New Shorter Oxford English Dictionary*, vol. 2, at 2557 (1993 ed.)

²⁹Agriculture Agreement, preamble.

foregone) not involving transfers from consumers and (b) the support in question shall not have the effect of providing price support to producers. Direct payments under the 2002 Act meet these basic criteria, and the expired production flexibility contract payments under the 1996 Act met these criteria as well.

62. As noted in the US first written submission, direct payments under the 2002 Act are support provided through a publicly-funded government programme not involving transfers from consumers. Under Section 1103 of the 2002 Act, the Secretary of Agriculture “shall make direct payments to producers on farms [including landowners where no production occurs] for which payment yields and base acres are established,” and, under Section 1601 of the Act, the Secretary “shall use the funds, facilities, and authorities of the Commodity Credit Corporation to carry out this title.” Thus, no transfers from consumers are involved.³⁰

63. Direct payments under the 2002 Act also do not have the effect of providing price support to producers. Direct payments augment the income of persons on farms based on historic acres and yields. They are not made to support any “applied administered price” for upland cotton (or that for any other commodity), for example, by increasing upland cotton demand or reducing upland cotton supply.³¹ To-date, Brazil has not contested that US direct payments satisfy both “basic criteria” under paragraph 1.

64. As set out in the US answer to Question 15 from the Panel, the expired production flexibility contract payments are not within the Panel’s terms of reference. Nonetheless, as we shall explain in more detail in our rebuttal submission, these payments too satisfy the “basic criteria” referred to in paragraph 1 of Annex 2. Production flexibility contract payments provide support through a publicly-funded government programme not involving transfers from consumers.³² In addition, production flexibility contract payments did not have the effect of providing price support to producers; these payments augmented the income of persons on farms based on historic acres and yields but were not made to support any “applied administered price” for upland cotton (or that for any other commodity). Again, Brazil has not contested that US production flexibility contract payments satisfy both “basic criteria” under paragraph 1.

31. If the first sentence of paragraph 1 of Annex 2 is not a stand-alone obligation, then must new, non- or minimally trade-distorting measures that do not conform to the criteria listed in Annex 2 be classified as non-Green Box? BRA, USA

65. As set out in the US answer to Question 29 from the Panel, the United States views the first sentence of paragraph 1 as an obligation in that it establishes a “fundamental requirement” for green box measures under Annex 2. This obligation is met when measures conform to the basic criteria of the second sentence plus the applicable policy-specific criteria of paragraphs 6 through 13. If a new measure does not conform to the basic and applicable policy-specific criteria in Annex 2, it will not have the benefit of the presumption that it meets the fundamental requirement of the first sentence.

32. If the first sentence of paragraph 1 of Annex 2 expresses a general principle which informs the interpretation of the criteria in Annex 2, please explain how this affects the assessment of the direct payments programme's compliance with paragraph 6 of Annex 2. USA

³⁰ See US First Written Submission, para. 65.

³¹ See US First Written Submission, para. 66.

³² Federal Agricultural Improvement Act of 1996, Title I, § 161(a) (“Use of Commodity Credit Corporation. — The Secretary shall carry out this title through the Commodity Credit Corporation.”); *id.*, Title I, § 111 (providing for production flexibility contract payments).

66. As set out in the US answer to Question 29 from the Panel, the United States does not view the first sentence of paragraph 1 as merely setting out a general principle; according to its term, it establishes a “fundamental requirement” for green box measures under Annex 2. However, Annex 2 also indicates that measures that conform to the basic criteria of the second sentence plus the applicable policy-specific criteria of paragraphs 6 through 13 comply with that fundamental requirement. Thus, the first sentence of paragraph 1 provides important context for the interpretation of other provisions of Annex 2.

67. US direct payments satisfy the criteria set out in Annex 2 and therefore comply with the fundamental requirement of the first sentence of paragraph 1. As explained in the US answer to Question 30, US direct payments satisfy the two basic criteria under the second sentence of paragraph 1. In addition, as set out in the US first written submission,³³ direct payments satisfy the five policy-specific criteria set out in paragraph 6 of Annex 2 for decoupled income support.

68. The context provided by the first sentence of paragraph 1 indicates that Brazil’s argument that direct payments do not satisfy paragraph 6(b) because payments are eliminated or reduced if payment recipients harvest certain fruits or vegetables is wrong.³⁴ Brazil’s argument essentially is that paragraph 6(b) precludes a Member from requiring a recipient *not* to produce certain crops, rather than precluding a Member from requiring a recipient *to* produce certain crops. As indicated above, however, Brazil’s interpretation leads to a conflict between paragraph 6(b) and the fundamental requirement of the first sentence. That is, a measure that demonstrably meets that fundamental requirement (there are no trade-distorting effects or effects on production because production of no crop is allowed) would be inconsistent with paragraph 6(b) (the amount of payment would be based on the type of production – production of no crops – in a year after the base period). In the context of the first sentence of paragraph 1, then, paragraph 6(b) should be read to prevent a Member from requiring a recipient *to produce* certain crops. US direct payments do not require a recipient to produce upland cotton or any other crop in order to receive payment.

"do not grant support to a specific commodity"

33. According to the United States' interpretation of the word "grant", when can a Member claim that a measure is not exempt from action under Article 13(b)? What if the measure is enacted annually? Can the Member obtain a remedy in respect of that measure under the DSU? USA

69. The United States has interpreted the word “grant” according to its ordinary meaning: to “bestow as a favour” or “give or confer (a possession, a right, etc.) formally.”³⁵ Because the phrase “such measures do not grant support to a specific commodity” is expressed in the present tense, we have explained that this criterion indicates that whether measures currently in effect are exempt from actions depends upon the support they currently grant.³⁶ For example, whether payments under the 2002 Act can be challenged in the WTO at this time requires an examination of the product-specific support such measures currently grant (understood to be as of the date of the panel request or panel establishment), not the support measures granted 1, 2, or 3 years ago. A finding of a Peace Clause breach by current measures would allow a Member to proceed with an action based on Peace Clause-specified provisions and potentially obtain remedies with respect to those current subsidies.

70. A Member can make the claim that a measure is not exempt from action under Article 13(b) when the Member believes the measures at issue fail to conform to the Peace Clause, including that the Member believes the measure provides support in excess of that decided in 1992. It would not

³³US First Written Submission, para. 67.

³⁴See also US Answer to Question 25 from the Panel.

³⁵*The New Shorter Oxford English Dictionary*, vol. 1, at 1131 (fourth & fifth definitions).

³⁶US First Written Submission, paras. 79-81.

matter whether the measure were enacted annually. If there were a finding of a breach of the Peace Clause, then the complaining party could obtain a remedy in the form of a recommendation to bring the measure into conformity with the WTO agreements.

71. The issue of when a Member can claim that a measure is not exempt from action highlights the difficulty in adopting Brazil's interpretation that *only* budgetary outlays are relevant to the Peace Clause comparison. In the case of US domestic support measures, budgetary outlays are not known ahead of time. Accordingly, Brazil could only provide *estimates* of marketing year 2002 budgetary outlays in its first submission, explaining that "the evidence to tabulate the support granted to upland cotton during MY 2002 is not yet complete as the marketing year does not end until 31 July 2003."³⁷ Brazil has not demonstrated that US product-specific budgetary outlays for upland cotton exceeded marketing year 1992 outlays as of the time of its panel request, as of the time of panel establishment, nor, indeed, as of today.³⁸

72. This problem is not presented when one looks at the support *as decided by* US domestic support measures. Because those measures, both in 1992 and today, set a rate of support (72.9 cents per pound during marketing year 1992; 52 cents per pound during marketing year 2002), the level of support is known at the outset (or even in advance) of the relevant crop year in which payments are made, permitting a rapid challenge and perhaps panel findings before a given crop year is over. Thus, a Member *would* be able to claim that a current measure is not exempt from action under Article 13(b) and *would* be able to obtain a remedy under the DSU.

35. Does a failure by a Member to comply in a given year with either the chapeau of Article 13(b) or the proviso in subparagraph (ii) of Article 13(b) impact its entitlement to benefit in an earlier or a later year from the exemption from action provided by Article 13(b)? BRA, USA

73. A failure by a Member to comply in a given year with either the chapeau of Article 13(b) or the proviso in subparagraph (ii) of Article 13(b) would only lift the exemption from action for those measures for the year of that breach. Measures (subsidies) in a later year would remain exempt from action so long as those measures in the given year comply with the conditions in Article 13(b)(ii).

74. This conclusion flows from the text of the Peace Clause as well as the nature of the subsidies challenged by Brazil. The universe of measures exempt from actions under Article 13(b)(ii) is "domestic support measures that conform fully to the provisions of Article 6 of this Agreement including direct payments that conform to the requirements of paragraph 5 thereof, as reflected in each Member's Schedule, as well as domestic support within *de minimis* levels and in conformity with paragraph 2 of Article 6." Because the fundamental commitment under Article 6 is to limit domestic support as measured by the Current Total Aggregate Measurement of Support to a Member's final bound commitment level, and that commitment is judged on a year-by-year basis³⁹, a Member may breach its commitments under Article 6 in one year and come back into compliance in the following year. Thus, conformity with this element of Article 13 must be judged on a year-by-year basis.

75. The proviso to Article 13 states that such measures shall be exempt from actions "provided that such measures do not grant support to a specific commodity in excess of that decided during the 1992 marketing year." Thus, with respect to past subsidies (and putting aside the issue of whether there is a measure that can be challenged under the DSU), the Peace Clause proviso would require an

³⁷Brazil's First Written Submission, para. 149.

³⁸See US Answer to Question 67 from the Panel.

³⁹Agriculture Agreement, Article 6.3 ("A Member shall be considered to be in compliance with its domestic support reduction commitments *in any year* in which its domestic support in favour of agricultural producers expressed in terms of Current Total AMS does not exceed the corresponding annual or final bound commitment level specified in Part IV of the Member's Schedule.") (emphasis added).

examination of the support those measures were granting as of the time such measures were in existence. Were the Peace Clause breached in any particular year, a Member could bring an action against such measure (subsidy), but only for the year of the breach. For example, where subsidies were provided on a yearly basis, a Member could breach the Peace Clause in one year in which the support such measures grant is in excess of that decided during the 1992 marketing year but could be in conformity in the following year if support were again within the 1992 marketing year level. Only the subsidies for the year in which the Peace Clause were breached would not be exempt from actions.

76. Finally, we note that payments under the 2002 Act are recurring subsidies, expensed in the crop year to which they apply and superseded by new payments in the following crop year.⁴⁰ (So too were past payments under the expired 1996 Act.) Thus, whether such measures conform fully to Article 6 and do not grant support in excess of that decided during the 1992 marketing year – that is, whether such measures are exempt from action under Article 13(b) – must be judged on a year-by-year basis. A breach of the Peace Clause in any particular year would allow a Member to bring an action against such measures, but only for the year of the breach.

36. Does a failure by a Member to comply with Article 13(b) in respect of a specific commodity impact its entitlement to benefit in respect of other agricultural products from the exemption from action provided by Article 13(b)? BRA, USA

77. No. For example, were the Panel to find a breach of the Peace Clause because the product-specific support US measures grant for upland cotton is in excess of that decided during the 1992 marketing year, this would not remove Peace Clause protection for support for soybeans (or any other commodity). In any subsequent action, a complaining Member would have to demonstrate that the challenged measures breach the Peace Clause with respect to that commodity and support.

37. In the United States' view, why did the drafters not use the exact term "product-specific" in Article 13(b)(ii)? USA

78. It is not possible to determine exactly why the drafters of Article 13(b)(ii) did not use the term “product-specific support” in place of “support to a specific commodity.” Nonetheless, the phrase “support to a specific commodity” must be interpreted according to its ordinary meaning, in context, and in light of the object and purpose of the Agreement. As the United States has explained, this phrase means “product-specific support.”⁴¹ We note that while it is no doubt a good *drafting* rule to use one and only one term for any given concept in an agreement, the drafters’ failure to follow that rule does not alter a treaty *interpreter’s* obligation to interpret under the customary rules of public international law the words that actually are in the treaty.

79. Further, it is not surprising that this exact phrase is not used in the Peace Clause. The phrase “product-specific support” is not a defined term to be found in Agriculture Agreement Article 1. Not surprisingly, then, in different provisions the Agriculture Agreement uses different words to describe the concept of product-specific support. For example, in Article 1(a), the basic definition of product-specific support (although not identified as such) is given as “support . . . provided *for* an agricultural product in favour of the *producers* of the basic agricultural product.” In Article 1(h), the Agreement again refers to product-specific support not by using that term but by using the words “support for basic agricultural products.”⁴² None of these references to “product-specific support” even uses the term “specific” whereas the phrase “support to a specific commodity” contains all three elements of that phrase (that is, product, specific, and support), using “commodity” in place of

⁴⁰ See US Answer to Question 15 from the Panel.

⁴¹ US First Written Submission, paras. 77-78.

⁴² Similarly, in Annex 3, paragraph 6, the Agreement refers to a “product-specific” AMS not by using those words but by using the phrase “for each basic agricultural product, a specific AMS shall be established.”

“support.”⁴³ The use of the phrase “support to a specific commodity” in the Peace Clause to refer to “product-specific support” is not remarkable in light of these multiple examples of different words in the Agreement that describe the same concept.⁴⁴

38. Given the fact that subsidies available for more than one product could have various effects on production, how does the United States demarcate between product-specific support and non-product specific support ? USA

80. The phrase “support to a specific commodity” in the Peace Clause proviso, read according to its ordinary meaning, in context, and in light of the object and purpose of the Agreement, means “product-specific support.” The United States finds the demarcation between product-specific and non-product-specific support in the Agriculture Agreement. Specifically, Article 1(a) defines the universe of support making up the Aggregate Measurement of Support as follows:

“Aggregate Measurement of Support” and “AMS” mean the annual level of *support*, expressed in monetary terms, *provided for an agricultural product in favour of the producers of the basic agricultural product or non-product-specific support provided in favour of agricultural producers in general*, other than support provided under programmes that qualify as exempt from reduction under Annex 2 to this Agreement . . . (italics added).

Article 1(h), which defines the “Total Aggregate Measurement of Support,”⁴⁵ and paragraph 1 of Annex 3, explaining the calculation of the Aggregate Measurement of Support⁴⁶, also distinguish between product-specific and non-product-specific support, without providing additional detail to that found in Article 1(a).

81. Article 1(a), therefore, provides the basic demarcation between product-specific and non-product-specific support; as mentioned at the first panel meeting, Brazil has not contested this point. Product-specific support, then, is “support . . . provided for an agricultural product in favour of the producers of the basic agricultural product.” This definition contains two elements. First, the support must be provided “*for an agricultural product*,” which suggests that the subsidy is given “in favour of”⁴⁷ a product and not in respect of criteria not related to the product or in respect of multiple products. Second, such support is “in favour of the *producers of the basic agricultural product*,”

⁴³Again, the use of the term “commodity” in place of “product” may result from the unique negotiating history of the Peace Clause. While the term “product” is used exclusively elsewhere in the Agreement, in the course of the Uruguay Round agriculture negotiations, the term “commodity” had been commonly used. *See, e.g.,* Framework Agreement on Agriculture Reform Programme, Draft Text by the Chairman, MTN.GNG/NG5/W/170, paras. 3, 5, 6, Annex I (11 July 1990). Despite the fact that the Peace Clause uses “commodity” in place of “product,” Brazil has not suggested that “commodity” should be interpreted as anything other than agricultural “products” subject to the Agreement.

⁴⁴The United States also notes that under paragraph 1 of Annex 3, non-product-specific support is to be aggregated into one separate AMS, which supports the notion that non-product-specific support is *not* to be allocated to specific products, contrary to what Brazil urges the Panel to do here.

⁴⁵Agriculture Agreement, Article 1(h) (“‘Total Aggregate Measurement of Support’ and ‘Total AMS’ mean the sum of all domestic support provided in favour of agricultural producers, calculated as the sum of all aggregate measurements of *support for basic agricultural products*, all *non-product-specific aggregate measurements of support* and all equivalent measurements of support for agricultural products . . .”).

⁴⁶Agriculture Agreement, Annex 3, paragraph 1 (“Subject to the provisions of Article 6, an Aggregate Measurement of Support (AMS) shall be calculated *on a product-specific basis for each basic agricultural product* receiving market price support, non-exempt direct payments, or any other subsidy not exempted from the reduction commitment (‘other non-exempt policies’). *Support which is non-product specific shall be totalled into one non-product-specific AMS* in total monetary terms.” (emphasis added)).

⁴⁷*The New Shorter Oxford English Dictionary*, vol. 1, at 996 (1993 ed.) (definition of “for”: “in favour of”; “[w]ith the purpose or result of benefitting”).

which suggests that subsidy benefits those who produce the product – that is, production is necessary for the support to be received.

82. Article 1(a) explains non-product-specific support as “support provided in favour of agricultural producers in general.” That is, non-product-specific support is not support provided “for an agricultural product” and is not support in favour of “the *producers* of the basic agricultural product” but rather is support in favour of agricultural producers “generally.”⁴⁸ Thus, read according to its ordinary meaning and in the context of Article 1(a), non-product-specific support is a residual category of support covering those measures that do not fall within the more detailed criteria set out in the definition of product-specific support.

83. Finally, we note Brazil’s argument that “[t]he term ‘product-specific’ that the United States seeks to read into Article 13(b)(ii) has a very technical and particular meaning as set out in Article 6(4), and Annex 3 to the Agreement on Agriculture.”⁴⁹ As explained above, while both of these provisions use the term “product-specific” as well as “non-product-specific,” the Panel will search these provisions in vain for a “technical and particular meaning” of either of these terms. Brazil fails to direct the Panel’s attention to the only explanation of the meaning of those terms, Article 1(a), perhaps because this explanation of the “technical and particular meaning” of product-specific support suggests that several of the measures challenged by Brazil provide non-product-specific support and are not part of the comparison under the Peace Clause proviso.

39. If "such measures" in Article 13(b)(ii) refers to all those in the chapeau of Article 13(b), why are they not all included in the potential comparisons with 1992? In what circumstances can measures which grant non-product specific support lose exemption from action under Articles 5 and 6 of the SCM Agreement and Article XVI of GATT 1994? USA

84. The introductory phrase of Article 13(b) establishes the full universe of measures that are potentially exempt from actions under this provision – that is, domestic support measures “that conform fully to the provisions of Article 6.” The phrase “such measures” in Article 13(b)(ii) occurs in the proviso, and the use of the word “such” refers back to those measures identified in the introductory phrase. However, the type of support that must be compared pursuant to the proviso is set out by the *text* of the proviso: the comparison is not between the *total* (product-specific and non-product-specific) support provided by all measures that existed in 1992 versus those that exist currently; rather, the proviso comparison is between the “support to a specific commodity” that challenged measures grant versus that decided during the 1992 marketing year.

85. With respect to Article 13(b), then, the Peace Clause has two tiers of analysis and effect. First, non-green box domestic support measures collectively lose Peace Clause protection if they do not conform fully to the provision of Article 6 – that is, if they exceed a Member’s domestic support commitment level. Second, even if a Member’s Current Total Aggregate Measurement of Support is within the reduction commitment, the support to a specific commodity can still lose its Peace Clause protection if it exceeds the level decided during marketing year 1992. This second tier was intended to prevent a Member from increasing its non-green box support to a specific commodity while staying within the domestic support commitment level. When a Member *has* disciplined its product-specific support, however, by staying within the level decided during the 1992 marketing year (as the United States has done), it is entitled to the benefit of observing that commitment.

86. Finally, we note that Brazil’s interpretation of the proviso calls for allocating support from all non-green box measures to an agricultural product regardless of whether that support is product-

⁴⁸ “In general” means “in general terms, generally” and “as a rule, usually.” *The New Shorter Oxford English Dictionary*, vol. 1, at 1073 (1993 ed.).

⁴⁹Brazil’s Opening Oral Statement at the First Panel Meeting, para. 16.

specific or non-product-specific. This analysis has no foundation in the Agriculture Agreement. In fact, Brazil has not followed its own approach through to its logical conclusion: as alluded to by Question 41 from the Panel, presumably Brazil could have taken *all* non-product-specific support provided by the United States and allocated some portion of that support to upland cotton producers. Brazil has not done so, but there is no basis in the Agreement to distinguish the non-product-specific support Brazil excluded from the non-product-specific support Brazil *included* for purposes of its Peace Clause analysis (for example, counter-cyclical payments and crop insurance). The only basis to distinguish whether a measure provides “support to a specific commodity” that is found in the Agriculture Agreement is to rely on the distinction between product-specific and non-product-specific support as explained in Article 1(a).

43. What are the precise differences between deficiency payments and counter-cyclical payments that lead you to classify the former as product-specific and the latter as non-product specific? How do you classify market loss assistance payments? USA

87. As indicated in the US answer to Question 38 from the Panel, Article 1(a) of the Agriculture Agreement provides the demarcation between product-specific and non-product-specific support. The definition of product-specific support contains two elements. First, the support must be provided “*for an agricultural product,*” which suggests that the subsidy is given in respect of a product and not in respect of criteria not related to the product or in respect of multiple products. Second, such support is “in favour of the *producers of the basic agricultural product,*” which suggests that subsidy recipients are those who produce the product – that is, production is necessary for the support to be received. Non-product-specific support is a residual category of “support provided in favour of agricultural producers in general” – that is, “generally.”

88. In light of these definitions, it follows that deficiency payments under the 1990 Act were product-specific support whereas counter-cyclical payments are non-product-specific. The relevant differences may be summarized as follows:

Deficiency Payments	Counter-Cyclical Payments
Farmer must plant upland cotton to receive payment	No requirement to plant upland cotton (or any crop)
Payment based on acres “planted for harvest” to upland cotton in that crop year	Payment based on historical “base acres” irrespective of acres currently planted to upland cotton

In short, deficiency payments required production of upland cotton whereas counter-cyclical payments do not. Thus, deficiency payments were support *for* upland cotton in favour of *the producers* of upland cotton.

89. In order to receive a deficiency payment, a producer was *required* to plant upland cotton for harvest. The “farm programme payment acreage” for an individual farm – that is, the acres on the farm for which the producer would receive a deficiency payment in a given crop year – was defined as “the smaller of the maximum payment acreage or *the acreage planted to the crop on the farm for harvest* within the permitted acreage of the crop of the farm.”⁵⁰ That is, a farmer would be paid on the acres planted to upland cotton for harvest up to the maximum payment acreage. Under the programme regulations, “crop acreage planted for harvest” was generally defined as “[t]he acreage

⁵⁰ Code of Federal Regulations § 1413.108(d) (1 Jan. 1993) (emphasis added) (Exhibit US-3); 7 US Code § 1444-2(c)(1)(B)(i) (1992 Supp.) (4 January 1993) (Exhibit US-5).

harvested.”⁵¹ Thus, in a given crop year, production was required to receive a deficiency payment, and the amount of the deficiency payment was based on the acreage on which upland cotton was harvested. Thus, both elements of the definition of product-specific support in Article 1(a) are satisfied. The deficiency payment was support for an agricultural product in favour of the producers of the product because recipients had to have planted upland cotton for harvest to receive payment in a given crop year.

90. On the other hand, counter-cyclical payments are decoupled from production requirements. Counter-cyclical payments are made to persons with farm acres that were devoted to production of any of a number of crops, including upland cotton, during an historical base period. That base period was defined in the 2002 Act and is fixed for the life of the legislation (that is, for marketing years 2002-2007).⁵² However, a person with “upland cotton base acres” need not produce upland cotton (nor any other particular crop) to receive the counter-cyclical payment. A person with “upland cotton base acres” also need not produce any crop at all. Thus, counter-cyclical payments do not satisfy the definition of product-specific support: they are not payments *for* an agricultural product in favour of *the producers* of the product since *no production of any product, including upland cotton, need occur for payment*.

91. As indicated in our 1999 WTO domestic support notification (G/AG/N/USA/43), the United States believes that market loss assistance payments are non-product-specific amber box support. As with production flexibility contract payments, market loss assistance payments were made to persons with farm acres that previously had been devoted to production of certain crops, including upland cotton, during an historical base period. No production of upland cotton or of any other crop was required to receive payment, and no production was required at all. Thus, these payments do not meet the definition of product-specific support in Annex 1(a).

92. However, the United States did notify these payments as amber box because they were made in response to low prevailing commodity prices. As such, the United States does not consider that they conform to the criterion in paragraph 6(c) of Annex 2 that the amount of decoupled income support payments “in any given year shall not be related to, or based on, the prices, domestic or international, applying to any production undertaken in any year after the base period”. We note that while Brazil has included market loss assistance payments in its Peace Clause comparison, it has not contested the US position (as evidenced by G/AG/N/USA/43) that these payments are non-product-specific amber box support.⁵³

45. If the Panel considered that Step 2 payments paid to exporters were an export subsidy, would the United States count them as domestic support measures for the purposes of Article 13(b)? Please verify Brazil's separate data for Step 2 export payments and Step 2 domestic payments in Exhibit BRA-69 or provide separate data. BRA, USA

⁵¹7 Code of Federal Regulations § 1413.4(b) (1 Jan. 1993) (Exhibit US-3). Under the 1990 Act, there were so-called 50-92 provisions, under which a producer could devote part of the maximum payment acreage (that is, 85 per cent of the established crop acreage base less any acreage under an acreage reduction programme) to conserving uses and still receive deficiency payments on the acreage. To take advantage of that provision, the producer was still required to plant upland cotton for harvest on *at least* 50 per cent of the maximum payment acreage. 7 US Code § 1444-2(c)(1)(D)(ii) (1992 Supp.) (4 Jan. 1993) (“To be eligible for payments . . . the producers on a farm must actually plant upland cotton for harvest on at least 50 per cent of the maximum payment acres for cotton for the farm.”) (Exhibit US-5).

⁵²By way of contrast, under the deficiency payment program, “base acres” were determined by a farmer’s yearly upland cotton planting decisions. Base acres were defined as “the average of the acreages planted and considered planted to such crop for harvest on the farm in each of the 3 crop years preceding such crop year.” 7 Code of Federal Regulations § 1413.7(c) (1 Jan. 1993) (Exhibit US-3).

⁵³See Brazil’s First Written Submission, paras. 60-62.

93. If the Panel were to conclude that the Step 2 programme and payments made thereunder could be separated into domestic and export components, and the export component were deemed to be an export subsidy, logically, that component would no longer constitute domestic support. Therefore, that measure would not form part of an analysis under Article 13(b), but rather would fall under Article 13(c). For data relating to Step 2 payment by fiscal year and use, please see the US answer to Question 104 from the Panel.

46. What is the relevance, if any, of the concept of "specificity" in Article 2 of the SCM Agreement and references to "a product" or "subsidized product" in certain provisions of the SCM Agreement to the meaning of "support to a specific commodity" in Article 13(b)(ii) Agreement on Agriculture? BRA, USA

94. The concept of specificity in Article 2 of the Subsidies Agreement is entirely unrelated to the meaning of "support to a specific commodity" in Article 13(b)(ii) of the Agreement on Agriculture. Generally, under Article 2 of the Subsidies Agreement, a subsidy is specific if it is limited, in law or in fact, to "an enterprise or industry or group of enterprises or industries." The relevant context for "support to a specific commodity" is found in Articles 1(a), 1(h), 6.4, and Annex 3 of the Agriculture Agreement.

"in excess of that decided during the 1992 marketing year"

47. Where does Article 13(b)(ii) require a year-on-year comparison? BRA, USA

95. Please see the US answer to Question 35 from the Panel for a reply to this question.

48. Does Article 13(b)(ii) require a comparison of support granted with support decided? How could such a comparison be made? BRA, USA

96. The proviso to Article 13(b)(ii) requires a comparison of the product-specific support that challenged measures grant (in this case, for upland cotton) to the product-specific support decided during the 1992 marketing year. The United States agrees with Brazil that the Peace Clause proviso requires an apples-to-apples comparison. However, while Brazil's proposed comparison (the budgetary outlays that may be allocated to a commodity, whether product-specific or non-product-specific) has no grounding in the text or context of the Peace Clause, the United States believes the basis for this comparison is established by the use of the word "decided."

97. The term "decided" is not explicitly defined in the Agreement and is not used elsewhere in the Agriculture Agreement nor in the Subsidies Agreement to refer to support or subsidies. Members' unique choice of words must be given meaning. "Decide" means to "[d]etermine on as a settlement, pronounce in judgement" and "[c]ome to a determination or resolution *that, to do, whether*."⁵⁴ Thus, the basis for the comparison under the Peace Clause proviso is the product-specific support that was "determined" or "pronounced" during the 1992 marketing year. US measures "decided" product-specific support for upland cotton in terms of a rate of 72.9 cents per pound through the combination of marketing loans and deficiency payments. Thus, to make an apples-to-apples comparison, this rate of support must be compared to the rate of support that challenged measures "grant."

98. Contrary to Brazil's assertion, the use of the term "grant" does not compel an examination of budgetary outlays. The ordinary meaning of "grant" is to "bestow as a favour" or "give or confer (a possession, a right, etc.) formally."⁵⁵ Thus, the use of the term "grant" would permit an evaluation of the rate of support that challenged measures "give or confer . . . formally". Brazil's reference to

⁵⁴*The New Shorter Oxford English Dictionary*, vol. 1, at 607 (first and third definitions) (italics in original).

⁵⁵*The New Shorter Oxford English Dictionary*, vol. 1, at 1131 (fourth & fifth definitions).

footnote 55 of the Subsidies Agreement⁵⁶ is not pertinent as this is one of several Subsidies Agreement references to a *Member* granting a *subsidy*,⁵⁷ which differs from the Peace Clause phrase, “such *measures* do not grant support”. More importantly, Members did not choose to use the word “granted” in place of “decided”, and a valid interpretation must make sense of that choice rather than reading it out of the Agreement. In addition, had Members intended the Peace Clause comparison to be made *solely* on the basis of budgetary outlays, they could have used that term. After all, “budgetary outlays” is a defined term in Article 1(c) and repeatedly referred to in the Agreement.⁵⁸

99. Thus, the comparison of the product-specific support “decided” during the 1992 marketing year to the support challenged measures “grant” must be made on the terms established by US measures themselves. The United States decided to ensure producer support at a rate of 72.9 cents per pound of upland cotton during the 1992 marketing year. In this case, the comparison presents no difficulty because the challenged measures also grant a rate of support (52 cents per pound). Because the latter is not in excess of the former, challenged US domestic support measures are exempt from actions pursuant to Article 13(b)(ii).

50. Please provide any written drafting history which could shed light on why the proviso was added to what is now Article 13(b)(ii) and, in particular, why both words "grant" and "decided" were used. USA

100. The United States is not aware of any written drafting history on this point.

51. Could the United States please comment on the interpretation advanced by the EC, in paragraphs 16 and 18 of its oral statement, of the words "decided during the 1992 marketing year"? USA

101. The United States agrees with parts of the interpretation advanced by the EC. The Communities too see the use of the term “decided” in the Peace Clause as notable and suggest that it compels an examination of “an amount of support adopted by some form of decision”. The Communities argues that a Member cannot be deemed to have “decided” all of the “applications for support under a particular programme” (as is implied by an examination of budgetary outlays) and that the term “decided” cannot “set up a comparison between domestic support [actually] granted in 1992 and domestic support granted in a more recent period”. The United States agrees with these statements.

102. The Communities also advance argumentation that may not flow from the ordinary meaning of the term “decided.” For example, the Communities suggests that the term “implies a one-off decision”, without further explanation. It would appear that the support “decided” during a marketing

⁵⁶See Subsidies Agreement, fn. 55 (“For a developing country Member not granting export subsidies as of the date of entry into force of the WTO Agreement, this paragraph shall apply on the basis of the level of export subsidies granted in 1986.”).

⁵⁷See, e.g., Subsidies Agreement, Article 2.1(c) (“Such factors are: . . . the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy”); *id.*, Article 3.2 (“A Member shall neither grant nor maintain [prohibited] subsidies referred to in paragraph 1.”); *id.*, Article 4.1 (“Whenever a Member has reason to believe that a prohibited subsidy is being granted or maintained by another Member, such Member may request consultations with such other Member.”); *id.*, Article 7.1 (“Except as provided in Article 13 of the Agreement on Agriculture, whenever a Member has reason to believe that any subsidy referred to in Article 1, granted or maintained by another Member, results in injury to its domestic industry, nullification or impairment or serious prejudice, such Member may request consultations with such other Member.”); *id.*, Article 9.2 (“Upon request for consultations under paragraph 1, the Member granting or maintaining the subsidy programme in question shall enter into such consultations as quickly as possible.”); *id.*, Article 25.2 (“Members shall notify any subsidy as defined in paragraph 1 of Article 1, which is specific within the meaning of Article 2, granted or maintained within their territories.”).

⁵⁸See Agriculture Agreement, Articles 3.3, 9.2; *id.*, Annex 3, paras. 2, 10, 12, 13; *id.*, Annex 4, para. 2.

year could be made through more than one decision, however. In addition, the Communities suggests that this decision is one “in which support for a specific product is decided and allocated for future years.” While it may be that a Member decided support for a future year during the 1992 marketing year, forming the benchmark for the comparison under the Peace Clause proviso, it would also appear likely that a Member decided on a level of support for the marketing year during that marketing year. Thus, the support decided during the 1992 marketing year would not appear to be necessarily limited to support for future years.

52. Please comment on an interpretation of the words "decided during" in Article 13(b)(ii) that would read them as synonymous with the words "authorized during". BRA, USA

103. The ordinary meaning of the words “decided during” would be “determined or pronounced during” or “having come to a determination or resolution that or to do during.” The United States understands that the term “decided during” was intended to capture not just a decision during 1992 for 1992, but also, as the EC indicates, a decision in 1992 of the support to be granted in a future year, in particular the EC’s decision during 1992 for future years. The term “authorized during” would not appear to capture all of these dimensions of the term “decided during”. In fact, a measure could be “authorized” during 1992 based on a “decision” during an earlier year so the two terms are not synonymous.

54. Please identify all United States legal and regulatory and administrative instruments decided during the marketing year 1992, with the respective dates of decision, that decided support for upland cotton. BRA, USA

104. The level of support decided during marketing year 1992 was to ensure a rate of return to producers of 72.9 cents per pound. Numerous legal, regulatory, and administrative instruments “determined” or “pronounced” this support. This level of support was first determined or pronounced by the 1990 Act, which covered the 1991-1995 marketing years. This legislation stated that “[t]he established price for upland cotton shall not be less than \$0.729 per pound” for deficiency payments⁵⁹ and promised to make up the difference between that price and the higher of the (1) marketing loan rate or (2) market price. The 1990 Act was enacted on 28 November 1990. We note that the established price was set at “not less than” 72.9 cents per pound; that is, the Secretary of Agriculture was given some discretion to set the effective price so long as this did not fall below 72.9 cents. The Secretary, in fact, did not decide to alter this effective price prior to, during, or after the 1992 marketing year.

105. The Secretary decided on the marketing loan rate applicable for the 1992 crop via a series of regulations. A proposed rule was published on 13 September 1991, at 56 Federal Register 46574. The final decision on a loan rate of 52.35 cents per pound was announced on 31 October 1991, published on 20 April 1992, at 57 Federal Register 14326.⁶⁰ Those determinations applied to all marketings during marketing year 1992.

106. The United States decided to maintain the effective price for deficiency payments and loan rate for marketing loans at those levels during the 1992 marketing year as reflected in several published documents. The 1 January 1993, Code of Federal Regulations (Exhibit US-3) codified these levels of support.⁶¹ The 1992 Supplement to the US Code also codified the legislated effective price of “not less than” 72.9 cents per pound. In addition, the Department of Agriculture published an upland cotton fact sheet in September 1992 announcing that “[t]he 1992 target price [for deficiency payments] is 72.9 cents per pound” and the “1992 loan rate . . . is 52.35 cents per pound”.⁶²

⁵⁹7 US Code § 1444-2(c)(1)(B)(ii) (1992 Supp.) (4 Jan. 1993) (Exhibit US-5).

⁶⁰Exhibit US-2.

⁶¹7 Code of Federal Regulations § 1413.104(a) (1 Jan. 1993) (Exhibit US-3).

⁶²US Department of Agriculture, Upland Cotton Fact Sheet, at 2 (September 1992) (Exhibit US-17).

107. Finally, we note that in anticipation of the 1993 crop year the Department of Agriculture also initially pronounced the level of support for the 1993 crop year during the 1992 marketing year. On 24 March 1993, regulations were published at 58 Federal Register 15755 setting the marketing loan rate at 52.35 cents per pound and leaving undisturbed the effective price for deficiency payments at 72.9 cents per pound.⁶³ Thus, the support decided for the 1993 crop was the same as that decided for the 1992 crop: to ensure producer support of 72.9 cents per pound of upland cotton.⁶⁴

55. Please provide a copy of the instrument in which the rate of support for upland cotton during the marketing year 1992 was decided, indicating the date of the decision. USA

108. As indicated in the US answer to Question 54 from the Panel, the United States has provided copies of multiple legal, regulatory, and administrative instruments and publications reflecting the rate of support decided during marketing year 1992. These multiple decisions stem from the fact that an effective price and marketing loan rate were first published in advance of the 1992 marketing year in order to allow producers to become familiar with the programmes; subsequently, the Secretary of Agriculture decided not to change either the effective price (72.9 cents per pound) or the marketing loan rate (52.35 cents per pound), despite having the authority to do so.

56. Could the United States please explain how support granted under legislation that dates back to 1990 can have been support "decided during the marketing year 1992"? USA

109. Payments during the 1992 marketing year were made pursuant to the 1990 Act, which directed the Secretary of Agriculture to make marketing loan payments and deficiency payments (as well as Step 2 payments). The 1990 Act, however, was only the first decision on the level of support. The Act provided that the marketing loan rate could "not be reduced below 50 cents per pound".⁶⁵ The 1990 Act also stated that the "established price for upland cotton shall not be less than \$0.729 per pound".⁶⁶ Thus, the Secretary had discretion to alter those rates of support.

110. The Secretary decided to set the marketing loan rate at 52.35 cents per pound in April 1992 but also decided not to change the implementing regulations establishing the effective price for deficiency payments. Similarly, during the 1992 marketing year, the Secretary had the discretion *to raise* the deficiency payment target price above 72.9 cents per pound and *to raise* the marketing loan rate above 52.35 cents per pound but decided not to. Documents published during 1992 evidence this decision: the 1992 supplement to the United States Code published in January 1993 reflects the decision not to alter the statutory provisions relating to upland cotton rates. The 1993 Code of Federal Regulations was published in January 1993 and also reflects the decision not to alter the regulatory rate provisions. Finally, when the upland cotton fact sheet was published in September 1992, the effective price and marketing loan rate were left unchanged, reflecting the Secretary's decision not to change the level of support.

111. In this case, the support determined or pronounced by US measures during the 1992 marketing year was also the support determined or pronounced for the 1992 marketing year. This result is entirely consistent with the Peace Clause text; in fact, it provides certainty to both Members seeking to provide support within Peace Clause limits and Members seeking to understand whether the Peace Clause has been breached.

⁶³A proposed rule for the 1993 crop was published on 29 September 1992. The 1993 rates were announced on 2 November 1992, and published in the 24 March Notice.

⁶⁴We note that one distinction made by the 24 March 2003 regulations between the 1993 crop and the 1992 crop was that the acreage reduction program percentage was lowered from 10 per cent in 1992 to 7.5 per cent in 1993.

⁶⁵7 U.S.C. 1444-2(a)(1), (2)(A) (1992 Supp.) (Jan. 4, 1993) (Exhibit US-5).

⁶⁶7 U.S.C. 1444-2(c)(1)(B)(ii) (1992 Supp.) (Jan. 4, 1993) (Exhibit US-5).

112. Thus, the 1990 Act initially established a level of support applicable to the 1991-95 crops. The US Congress could have changed the 72.9 cents per pound level at any time during MY 1992, but it decided not to. The Secretary of Agriculture also had discretion to alter the level of support (that is, to raise it) but also decided not to. Thus, 72.9 cents per pound was decided and remained decided as the level of support for each day of the 1992 marketing year.

57. If the United States decided on a rate of support for MY1992, does that not mean that it decided on whatever budgetary outlay was required to meet that rate of support, even if the exact amount was not known at that time ? USA

113. The Peace Clause proviso establishes the benchmark for comparison: the support “decided” during the 1992 marketing year. To say that the United States “determined” or “pronounced” an indefinite amount of budgetary outlays would not fit those meanings of the term. The United States could also not have come to a “determination or resolution” to make any budgetary outlay since that outlay would be determined by market prices during the year, *not* by the US Government. To read support “decided” as encompassing not only the explicit rate of support set out in US measures but also “whatever budgetary outlay was required to meet that rate of support, even if the exact amount was not known at the time,” would also appear to make the Peace Clause comparison impossible. That is, because both during the 1992 marketing year and under the 2002 Act the support decided would be “whatever budgetary outlay was required to meet that rate of support,” both budgetary outlay “decisions” by the United States would appear to be unlimited, and one could not be in excess of the other. Alternatively, one could reason that a decision to provide whatever budgetary outlays would be necessary implies that the 1992 decided level would be higher because, even if prices fell to zero, the higher nominal level in 1992 would mean higher budgetary outlays.

114. The only support “decided” by the United States was the 72.9 cents per pound level of support. In effect, the United States provided a revenue floor for producers by guaranteeing a rate of income for plantings. The United States has never exceeded that level of incentive “for the commodity.” Brazil’s approach, which would ascribe to the United States a decision to make budgetary outlays resulting from differences between market prices and the level of support, is an effort to impose something akin to an AMS limit on US support for upland cotton. (We note, however, that Brazil cannot simply argue for calculating an AMS for upland cotton because that would exclude non-product-specific support, which Brazil wishes to include in the Peace Clause comparison, and would not require that support be measured through budgetary outlays.) Members considered and rejected any product-specific AMS limits in the Uruguay Round, however, and such a concept may not be overlaid onto the Article 13 language. The United States has introduced payments decoupled from production precisely to lower the incentive to produce the marginal pound of cotton and avoid exceeding the product-specific level of support of 72.9 cents per pound.

59. Should the rate of support as indicated in Article 13(b)(ii) include the market price? If so, why is it appropriate to include it in the comparison under Article 13(b)(ii)? BRA, USA

115. No, the market price is not relevant for purposes of the Peace Clause comparison. As indicated in the US answers to Questions 48 and 57 from the Panel, the benchmark for that comparison is the support “decided” during the 1992 marketing year. That support was decided by the United States as a rate of support: 72.9 cents per pound. The actual amount of expenditures necessary to provide that support depended on the market prices during the marketing year. However, these prices were not “determined” or “pronounced” by the United States and therefore cannot have been (or be) part of any US decision.

60. Can you provide information on support decided in 1992 and the years with which you believe it should be compared, on a per support programme / per unit of production/per

annum basis? If possible, please specify how, if at all, budget outlays may be transposed into units of production, and which units of production are best to use. BRA, USA

116. The United States has explained that the product-specific support decided during the 1992 marketing year for upland cotton was 72.9 cents per pound through the combined effect of the target price for deficiency payments and the loan rate for marketing loans. This rate was the only support “decided” by the United States as evidenced by the relevant legislation, regulations, and programme announcements. By comparison, the product-specific support that upland cotton support measures currently grant is only 52 cents per pound through the loan rate for the marketing loan programme.

117. The United States believes that any analysis that takes budgetary outlays into account necessarily will not reflect the support “decided” by the United States. Because US domestic support measures are largely dependent on a price-gap, budgetary outlays will reflect prevailing market prices during the applicable marketing year, prices the United States cannot decide. Budgetary outlays will also reflect, for the product-specific support that marketing loans grant, various *producer* decisions on programme participation, timing of receipt of payments, and production levels. Again, these factors cannot be decided by the United States. Thus, given the way in which the challenged US measures decide the level of support, the Peace Clause comparison may only be made on the basis of rates of support, not budgetary outlays.

61. Does the United States consider that Article 13(b)(ii) permits a comparison on any basis other than a per pound basis? USA

118. Article 13(b)(ii) requires that the benchmark for comparison be the support “decided” during the 1992 marketing year. The United States decided on an a rate of support of 72.9 cents per pound during the 1992 marketing year. Therefore, the evaluation must be whether challenged measures grant product-specific support in excess of that decided during the 1992 marketing year – that is, in excess of the 1992 rate of support. Were the relevant US domestic support measures structured differently, the term “decided” might imply a different comparison.

66. Could you please comment on the relative merits of each of the following calculation methods for the purposes of the comparison of support to upland cotton with 1992, irrespective of whether a particular measure should be included or excluded:

(a) Total budgetary outlays (Brazil's approach). USA

119. As stated in the US answer to Question 60 from the Panel, the United States believes that any analysis that takes budgetary outlays into account necessarily will not reflect the support “decided” by the United States. Because some US domestic support measures are dependent on a price-gap (for example, marketing loans), budgetary outlays will reflect prevailing market prices during the applicable marketing year, prices the United States cannot decide. Budgetary outlays will also reflect, for the product-specific support that marketing loans grant, various *producer* decisions on programme participation, timing of receipt of payments, and production levels. Again, these factors cannot be decided by the United States. Thus, given the way in which the challenged US measures decide the level of support, the Peace Clause comparison may only be made with respect to these measures on the basis of rates of support, not budgetary outlays.

(b) Budgetary outlays per unit of upland cotton: Could you please calculate and provide an estimate for the marketing years 1992 and 1999-2002, respectively, and draw attention to any factors/qualifications that the Panel would need to be aware of. BRA, USA

120. For the reasons stated in response to Question 66(a), any analysis involving budgetary outlays necessarily will not reflect the support “decided” by the United States. A budgetary outlays per unit

of upland cotton approach thus would not only be based on a faulty premise, but to calculate outlays per unit might also necessitate an *ex post* or retrospective analysis. Again, this cannot reflect the support “decided” by the United States.

(d) Per unit rate of support for upland cotton (Prof. Sumner's approach at the first session of the first substantive meeting). USA

121. The United States continues to examine Mr. Sumner's approach to calculating a per-unit subsidy rate. We will present a detailed critique of Mr. Sumner's analysis in our rebuttal submission. Here, we limit our comments to two points.

122. First, as with the budgetary outlays approach favoured by Brazil, this per unit rate of support analysis ascribes to the United States choices made by producers themselves. For example, the first line of Sumner's analysis of the deficiency payment programme stated: “The following qualifications and adjustments must [] be made to the level of support provided by the deficiency payment programme: (1) payments were made *only if a farm chose to participate* in the deficiency payment programme; in 1992, farms representing 11 per cent (1.64 million acres) of the total ‘effective’ upland cotton acreage base (14.9 million acres) *did not agree to participate in the programme* and hence cotton production on this land could not receive support.”⁶⁷ Sumner makes a similar argument and adjustment for the 1992 loan rate.⁶⁸

123. Attempting to adjust the per unit rate of support to take account of producers that chose not to participate in the programme is a serious conceptual error. In economic terms, a farmer that participated in the upland cotton programme received full programme benefits; a farmer who chose not to participate did not. Averaging these numbers produces a “per unit rate of support” that no cotton farmer ever could have expected to receive.

124. Nor could a Member have “decided” such a level of support. In legal terms, an individual producer's choices on programme participation do not reflect any decision by the US Government. Thus, estimated rates of support that reflect these producer decisions are not relevant to the Peace Clause analysis under Article 13(b)(ii). We will discuss other conceptual errors in Sumner's approach in our rebuttal submission.

125. In reviewing Sumner's analysis, the United States was particularly struck by another point. The Panel may recall Brazil commenting at the first panel meeting that Sumner's calculations were not entirely unfavourable to the US position. A look at Appendix Table 1 to Sumner's statement (Exhibit BRA-105) reveals why.

126. Even using Sumner's flawed calculations, if one excludes the non-product-specific support that Brazil is attempting to “allocate” to upland cotton from the table, Sumner's analysis supports the United States, not Brazil. That is, Sumner's estimated per unit rate of support was *lower* in every year from marketing year 1999 through marketing year 2002 than the level of support during marketing year 1992:

⁶⁷Exhibit BRA-105 (Statement of Mr. Daniel Sumner, para. 10) (emphasis added).

⁶⁸Exhibit BRA-105 (Statement of Mr. Daniel Sumner, para. 12).

Product-Specific Support in Sumner's per Unit Subsidy Rates (Cents per Pound) by Programme and Year					
	MY1992	MY1999	MY2000	MY2001	MY2001
Marketing Loan	44.34	50.36	50.36	50.36	52.00
Deficiency	13.25	na	na	na	na
Step 2	2.46	2.46	2.46	2.46	3.71
Cottonseed	na	0.97	2.27	na	0.61 ⁶⁹
Total	60.05	53.79	55.09	52.82	56.32

127. Thus, even were one to accept for purposes of argument Sumner's approach, comparing the product-specific support the challenged measures grant to the product-specific support decided during marketing year 1992 reveals that *in no marketing year from 1999 through 2002 did the level of support exceed the marketing year 1992 level*. Under Article 13(b)(ii), then, Sumner's own analysis reveals that US domestic support measures that conform fully to the provisions of Article 6 are exempt from actions based on Peace Clause-specified WTO subsidies provisions.

67. **The Panel requests the parties to calculate and submit estimates of the AMS for upland cotton for marketing years 1992, 1999, 2000, 2001 and 2002. For this purpose the parties are each requested to submit AMS calculations for upland cotton (using the budgetary-outlay/non-price gap methodology employed by the United States in respect of cotton in its DS Notifications (e.g., G/AG/N/USA/43) and using the formats and supporting tables in document G/AG/2) on the same basis as would be the case in calculating a product specific AMS for the purposes of the calculation of the "Total Current AMS" in any year in accordance with the relevant provisions, including as appropriate Article 1(a), (b) and (h), Article 6 and Annex 3 to the Agreement. BRA, USA**

128. The United States has calculated a product-specific Aggregate Measurement of Support for upland cotton for marketing years 1992, 1999, 2000, 2001, and 2002, as explained below. This table summarizes the results of those calculations, and the following paragraphs provide additional detail:

US Upland Cotton Aggregate Measurement of Support	
Marketing Year	AMS (US \$, millions)
1992	2,085
1999	2,262
2000	1,057
2001	2,804

⁶⁹The United States includes the cottonseed amount from the table without prejudice to our preliminary ruling request that the Panel find the 2003 cottonseed payment not to be within the scope of this dispute.

US Upland Cotton Aggregate Measurement of Support	
2002 ⁷⁰	970

129. For marketing year 1992, the United States has used official data on budgetary outlays⁷¹ to calculate the upland cotton Aggregate Measurement of Support, except for other product-specific support in the form of storage payments and interest subsidies. The latter payment amounts are based on estimates by the US Department of Agriculture. The calculations, in millions of US dollars, are as follows:

Crop year 1992 (estimate)	Payments	Source
Deficiency payments	1,017	US Department of Agriculture (USDA), Upland Cotton Fact Sheet (Ex. Bra-4)
Marketing loan gains / Certificate exchange gains	476	USDA budget data (Ex. Bra-6)
Loan deficiency payments	268	USDA budget data (Ex. Bra-76)
User marketing certificates	207	USDA, Upland Cotton Fact Sheet (Ex. Bra-4)
Commodity loan forfeit	(5)	USDA estimate
Other payments	122	USDA estimate of storage payments & interest subsidy
<i>Product-Specific AMS</i>	2,085	

130. To calculate the upland cotton Aggregate Measurement of Support for marketing year 1999, the United States has used official budgetary outlays data for loan deficiency payments, marketing loan gains, certificate exchange gains, user marketing certificates, and the 1999 crop year cottonseed payment. For storage payments and interest subsidies, we have used estimates by the US Department of Agriculture as notified to the WTO. The calculations, in millions of US dollars, are as follows:

⁷⁰As explained further below, the United States has calculated the 2002 Aggregate Measurement of Support for upland cotton as of the date of panel establishment, 18 March 2003.

⁷¹In light of the question from the Panel, we have used budgetary outlays to estimate payments.

Crop year 1999	Payments	Source
Marketing loan gains/ Certificate exchange gains	860	USDA budget data (Ex. Bra-55)
Loan deficiency payments	685	USDA, Upland Cotton Fact Sheet (Ex. Bra-4)
User marketing certificates	422	USDA, Upland Cotton Fact Sheet (Ex. Bra-4)
Cottonseed payments	79	G/AG/N/USA/43
Other payments	216	USDA estimate of storage payments & interest subsidy (G/AG/N/USA/43)
<i>Product-Specific AMS</i>	2,262	

131. To calculate the upland cotton Aggregate Measurement of Support for marketing year 2000, the United States has again used official budgetary outlays data for loan deficiency payments, marketing loan gains, certificate exchange gains, and user marketing certificates; the amounts set by legislation for the 2000 crop year cottonseed payments; and estimates by the US Department of Agriculture for storage payments and interest subsidies. The calculations are as follows:

Crop year 2000 (estimate)	Payments	Source
Marketing loan gains	61	USDA budget data (www.fsa.usda.gov/dam/BUD/estimatesbook.htm) ⁷²
Loan deficiency payments	152	USDA, Upland Cotton Fact Sheet (Ex. Bra-4)
User marketing certificates	236	USDA, Upland Cotton Fact Sheet (Ex. Bra-4)
Cottonseed payments	185	Public Law 106-224, §204(e) (20 June 2000); Public Law 107-25, § 6 (13 Aug. 2001)
Certificate exchange gains	360	USDA budget data (www.fsa.usda.gov/dam/BUD/estimatesbook.htm)
Other payments	63	USDA estimate of storage payments & interest subsidy
<i>Product-Specific AMS</i>	1,057	

132. For marketing year 2001, the United States has used estimates by the US Department of Agriculture for storage payments and interest subsidies and official data on budgetary outlays for all other payments to calculate the upland cotton Aggregate Measurement of Support. The calculations, in millions of US dollars, are as follows:

⁷²Exhibit US-18.

Crop year 2001 (estimate)	Payments	Source
Marketing loan gains	47	USDA budget data (www.fsa.usda.gov/dam/BUD/estimatesbook.htm)
Loan deficiency payments	744	USDA budget data (Ex. Bra-76)
User marketing certificates	196	USDA, Upland Cotton Fact Sheet (Ex. Bra-4)
Certificate exchange gains	1,750	USDA budget data (www.fsa.usda.gov/dam/BUD/estimatesbook.htm)
Other payments	68	USDA estimate of storage payments & interest subsidy
<i>Product-Specific AMS</i>	2,805	

133. For crop year 2002, the United States has provided unofficial data on budgetary outlays as of 18 March 2003, the date of establishment of the Panel, for marketing loan gains, certificate exchange gains, loan deficiency payments, and user marketing certificates. Because the crop year has just ended (as of 31 July 2003), official budgetary outlay data is not yet available. For the 2002 crop year cottonseed payment, the United States has used the amount set by legislation (\$50 million). We use a crop-year's-end estimate by the US Department of Agriculture for storage payments and interest subsidies. The calculation, in millions of US dollars, is as follows:

Crop year 2002 (estimate as of panel establishment)	Payments	Source
Marketing loan gains/ Certificate exchange gains	563	USDA unofficial data (www.fsa.usda.gov/pscad/answer82rnat.asp (18 March 2003)) ⁷³
Loan deficiency payments	202	USDA unofficial data (www.fsa.usda.gov/pscad/answer82rnat.asp (18 March 2003))
User marketing certificates	137	USDA unofficial data
Other payments	68	USDA estimate of storage payments & interest subsidy
<i>Product-Specific AMS</i>	970	

134. We note that it would not be appropriate for the Panel to examine payments made after the date of panel establishment, on which the Panel's terms of reference were set. Measures taken after the Panel was established cannot be within the Panel's terms of reference. However, for the Panel's convenience, we have also estimated an Aggregate Measurement of Support for the entire crop year 2002, using US Department of Agriculture projections of all payments with respect to the 2002 crop

⁷³See Exhibit US-19 (Marketing Year 2002 Loan Deficiency Payment and Price Support Cumulative Activity As of 3/12/2003). Upland cotton data is shown in the row marked "UP." The loan deficiency payment amount is shown in the third column, and the marketing loan gain and certificate exchange gain amounts are shown in the eighth column (second from left). This Report, the PSL-82R, provides weekly, unofficial data. Brazil provided the same report as Bra-55 but chose to present the report with data as of 13 June 2003.

year. These projections show no dramatic change from the unofficial budgetary outlays as of 18 March. The full-year 2002 crop year estimate, in millions of US dollars, is as follows:

Crop year 2002 (full-year estimate)	Payments	Source
Marketing loan gains	11	USDA estimate (www.fsa.usda.gov/dam/BUD/estimatesbook.htm) ⁷⁴
Loan deficiency payments	206	USDA estimate (www.fsa.usda.gov/dam/BUD/estimatesbook.htm)
User marketing certificates	217	USDA estimate (www.fsa.usda.gov/dam/BUD/estimatesbook.htm)
Cottonseed payments	50	Public Law 108-7, § 206 (24 Feb. 2003)
Certificate exchange gains	701	USDA estimate (www.fsa.usda.gov/dam/BUD/estimatesbook.htm)
Other payments	65	USDA estimate of storage payments & interest subsidy
<i>Product-Specific AMS</i>	1,250	

68. Could you please clarify the result of the calculations of, and the meaning of the title, in Appendix Table 1 "Estimated per unit Subsidy Rates by Programme and Year" in Annex 2 to Exhibit BRA-105, page 12. Why are the numbers calculated for marketing loans considered to be subsidies? Could the Panel, for example, read the "total level of support" (bottom line of the table) as the effective support price for upland cotton or the maximum rate of support for upland cotton? BRA, USA

135. The United States looks forward to reviewing Brazil's explanation of its Appendix Table 1 to Annex 2 to Exhibit BRA-105.

69. Can the United States confirm that the "marketing year" for upland cotton is 1 August to 31 July? Can the United States confirm the Panel's understanding that USDA data for the "crop year" corresponds to the "marketing year"? USA

136. The United States confirms that the "marketing year" for upland cotton is 1 August to 31 July.⁷⁵ In response to a question from the Panel at the first meeting, we also communicate that payments listed in the Upland Cotton Fact Sheet (Ex. Bra-4) are for monies spent with respect to cotton harvested in a particular crop year, not necessarily for payments made during the marketing year.

EXPORT CREDIT GUARANTEE PROGRAMMES

71. (a) Is an export credit guarantee a financial contribution in the form of a "potential direct transfer of funds or liabilities (e.g. loan guarantee)" within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement? Why or why not? Does it confer a benefit within the meaning of Article 1.1(b)? Why or why not? If so, to whom? USA

⁷⁴Exhibit US-19.

⁷⁵7 Code of Federal Regulations 1412.103.

(b) How, if at all, would these elements be relevant to the claims of Brazil, and the United States response thereto? BRA, USA

137. (a) For the reasons stated in its first written submission⁷⁶ and in response to Question 71(b), the United States does not believe that the appropriate analysis of the US export credit guarantee programme should begin with the Subsidies Agreement, much less Article 1 of that Agreement. The text of Article 10.2 defers WTO obligations for export credit guarantees until disciplines are internationally agreed, such as within the OECD or WTO. Under the Agriculture Agreement, the provisions of the Subsidies Agreement “apply subject to the provisions of this Agreement,”⁷⁷ and the export subsidy disciplines of Article 3.1(a) of the Subsidies Agreement expressly apply “[e]xcept as provided in the Agreement on Agriculture.”⁷⁸ Thus, the appropriate analysis would begin and end with Agriculture Agreement Article 10.2.

138. Even were the Subsidies Agreement relevant to US export credit guarantees, given that export credit guarantees are covered by item (j) of the Illustrative List of Export Subsidies, the appropriate mode of analysis under the Subsidies Agreement is to examine whether the programme is covering its long-term operating costs and losses.

139. (b) Article 3 of the SCM Agreement specifically states that Article 3.1(a), prohibiting export subsidies, applies “[e]xcept as provided in the Agreement on Agriculture”. Article 21.1 of the Agriculture Agreement states that “[t]he provisions of GATT 1994 and of other Multilateral Trade Agreements in Annex 1A to the WTO Agreement shall apply subject to the provisions of this Agreement”. Under Article 10.2 of the Agreement on Agriculture, the negotiators specifically deferred the application of export subsidy disciplines on agricultural export credit guarantee programmes like those of the United States. Any incidental “benefit” of any such measures is therefore irrelevant. Similarly, even if a particular (non-export credit) measure comprised a contribution and conferred a benefit for purposes of the Subsidies Agreement, to the extent the resulting subsidy was contingent on export performance, such export subsidy might nevertheless be permitted under the Agreement on Agriculture if within a Member’s applicable reduction commitment.

73. The Panel could arguably take the view that Articles 1 and 3 of the SCM Agreement were relevant in assessing the WTO-consistency of United States export credit guarantees. The United States has yet to submit any evidence or argumentation on this point, either as potential context for interpretation of the terms in Article 10 of the Agreement on Agriculture or in relation to Brazil's claims under the SCM Agreement. The Panel would therefore appreciate United States views in respect of this situation, and invites the United States to submit relevant argumentation and evidence. USA

140. The United States does not believe that Brazil has submitted evidence and argumentation that would establish a *prima facie* case in favour of Brazil’s claims, in particular in light of Article 10.2 of the Agriculture Agreement. However, the United States will review Brazil’s submissions, including its responses to these questions, and provide any further response in the US submission.

74. If the Panel decides to refer to provisions of the SCM Agreement for contextual guidance in the interpretation of the terms in Article 10 of the Agreement on Agriculture, should the Panel refer to item (j) or Articles 1 and 3 of the SCM Agreement or both? BRA, USA

⁷⁶US First Written Submission, paras. 167-170.

⁷⁷Agriculture Agreement, Article 21.1.

⁷⁸Subsidies Agreement, Article 3.1.

141. As the United States has argued, the first point of analysis is Article 10.2 of the Agreement on Agriculture, in which Members agreed that they would only provide export credit guarantees in conformity with internationally agreed disciplines, which they undertook to develop. That is, Article 10.2 indicates that no “internationally agreed disciplines” currently exist. The obligation with respect to export credit guarantees is, in effect, a work programme to establish a future discipline. Brazil has not contested that challenged US export credit guarantee programmes are within the scope of Article 10.2. Therefore, neither item (j) nor Articles 1 and 3 of the Subsidies Agreement are relevant to the Panel’s analysis of Article 10.2. We do note, however, that item (j) of the Illustrative List of Export Subsidies was agreed in the Uruguay Round, and, in fact, had previously formed part of the Illustrative List under the Tokyo Round Subsidies Code. Thus, the fact that Members had agreed on item (j) and yet, in Article 10.2, agreed to “undertake to work toward *the development* of internationally agreed disciplines to govern the provision of export credits, export credit guarantees” and, once agreed, only to provide export credit guarantee programmes “in conformity with” such developed and agreed disciplines, suggests that item (j) does *not* impose disciplines on export credit guarantees for agricultural goods.

142. Context for Article 10 is found in Article 9.1 of the Agreement on Agriculture, which describes specific practices that constitute export subsidies for purposes of the Agreement on Agriculture. Export credit guarantees were not listed among such practices. As to the practices described in Article 9.1, no recourse is necessary to Articles 1 and 3 of the SCM Agreement to determine whether a particular practice is an export subsidy. Article 1(e) of the Agreement on Agriculture defines an export subsidy only as a subsidy contingent on export performance. To determine the applicability of Article 10.1 to a particular measure not described in Article 9.1 first requires a determination whether a subsidy exists. In this regard, Article 1 of the SCM Agreement would provide relevant context.

75. The Panel's attention has been drawn to Article 14(c) of the SCM Agreement (see e.g. written third party submission of Canada) and to the panel report in DS 222 Canada-Export Credits and Loan Guarantees. How and to what extent are Article 14(c) of the SCM Agreement, and the cited panel report, relevant to the issue of whether or not the United States export credit guarantee programmes confer a "benefit"? What would be the appropriate market benchmark to use for any comparison? Please cite any other relevant material. BRA, USA

143. For reasons set out in more detail in the US answer to Question 71(b) and Question 71(c) from the Panel, the United States does not believe that Article 14(c) is relevant to the Panel’s analysis. An appropriate analysis of the US export credit guarantee programme begins and ends with Article 10.2 of the Agreement on Agriculture. Even were the Subsidies Agreement relevant to US export credit guarantees, the only appropriate mode of analysis under the Subsidies Agreement is to examine whether US export credit guarantee programmes are covering their long-term operating costs and losses under item (j) of the Illustrative List of Export Subsidies.

76. How does the United States respond to Brazil's statement that : "...export credit guarantees for exports of agricultural exports [sic] are not available on the marketplace by commercial lenders."? USA

144. Brazil is incorrect. Commercial insurers do offer export credit insurance covering agricultural commodities. According to a background paper on export credits prepared by the WTO Secretariat, “While guarantees could be unconditional, they usually have conditions attached to them, so that in practice there is little distinction between credits which are guaranteed and credits which are subject to insurance.”⁷⁹ However, for the sake of completeness we wish to note that such private insurance is structured differently than CCC credit guarantees. Most commonly, private insurers offer portfolio

⁷⁹See *Export Credits and Related Facilities*, G/AG/NG/S/13 (26 June 2000).

coverage, covering multiple customers and transactions for a particular exporter. Because the coverage is not based on individual transactions (like CCC's coverage), it may be difficult or impossible to discern which particular transactions involve agricultural commodities.

77. How does the United States interpretation of "long term operating costs and losses" in item (j) as claims paid give meaning to both "costs" and "losses"? Do claims paid represent "losses" or "costs" or both? If claims paid is represented by "losses", what would go into the "cost" element of item (j)? Could the United States expand on why it disagrees with the items which Brazil identifies for inclusion in the examination to be conducted under item (j)? USA

145. Item (j) applies to three different types of programmes: export credits, export credit guarantees, and insurance. In the case of the latter two types of programmes, the provider will necessarily incur claims from time to time. In the case of direct export credits (the first type of programme), the provider will experience defaults on occasion. To the extent such claims or defaults exceed revenue from whatever source it may be derived, the net result would be a loss arising from operations. In an accounting sense such result would constitute an "operating loss."

146. In addition, it is appropriate to identify and allocate costs necessary to operate such programmes. For example, the United States agrees that certain administrative expenses should be allocated to the operation of the export credit guarantee programmes, and an annual figure is attributed as administrative expense in the budget of the United States. Other costs necessary for the operation of a programme would constitute "operating costs" of such programme.

147. Were item (j) to be relevant in this dispute, therefore, that item compels an examination of losses derived from the operation of the programme plus the costs necessarily allocable to the programme for its operation. In the case of US export credit guarantee programmes, as reflected in paragraph 173 and accompanying tables of the US first written submission, the Commodity Credit Corporation (CCC) charges and receives premiums from applicants. In addition, CCC receives post-claim revenue through late payments and rescheduling. As reflected in the tables, with respect to cotton, such revenue exceeds the relevant claims experience. The United States has, therefore, not incurred an operating loss.

148. It is appropriate to allocate operating costs of the programme in the final analysis within the meaning of item (j). The United States disagrees, however, with the allegation of Brazil concerning interest allocation and the manner in which it attempts to ascribe figures from the US budget to operating costs for purposes of item (j). These items are addressed specifically in the US response to Question 81 from the Panel.

78. Can the United States provide supporting documentation for data used relating to "costs and losses" in paragraph 173? Could the United States confirm that the figures cited in paragraph 173 of its first written submission relate to the SCGP? Why did the United States cite these figures after stating that it is not possible to make any assessment of the long-term operating costs and losses of this programme? USA

149. The United States maintains a comprehensive electronic data base of export credit guarantee programme activity. The data base is updated on a regular basis and is the source of the data shown in paragraph 173 and accompanying table. Data is recorded in the system at the time of each transaction. These include such items as claim payments, recoveries, rescheduling agreements, and fees received.

150. As indicated in the tables accompanying paragraph 173, the figures shown in paragraph 173 relate to GSM-102 in the first table and SCGP in the second table. During the ten fiscal years reflected in the tables, no GSM-103 export credit guarantees were issued with respect to cotton.

79. In respect of what time periods does Article 13(c) require an assessment of conformity with Part V of the Agreement on Agriculture? How does this affect, if at all, your interpretation of Article 13(b)? BRA, USA

151. Article 13(c) applies to “export subsidies that conform fully to the provisions of Part V of th[e Agriculture] Agreement, as reflected in each Member's Schedule.” Part V of the Agreement, and in particular Article 8, establishes that “Each Member undertakes not to provide export subsidies otherwise than in conformity with this Agreement and with the commitments as specified in that Member's Schedule.” Those export subsidy reduction commitments, which are expressed in both export quantity and budgetary outlay terms, apply on a yearly basis.⁸⁰ Accordingly, a Member may be in conformity one year and not in conformity in another with regard to any particular commodity subject to reduction commitments.

152. If a Member has provided export subsidies to a particular commodity in any one year in excess of the applicable reduction commitments, then export subsidies for that commodity during such year would not “conform fully to the provisions of Part V”, and those subsidies would not have Peace Clause protection. In a subsequent year, a Member may again comply with its export subsidy commitments. Its export subsidies would then conform fully to Part V of the Agreement and would again receive Peace Clause protection.

153. Similarly, a failure by a Member to comply in a given year with the criteria in Article 13(b) would lift the exemption from action for those domestic support measures only for the year of the breach. Measures (subsidies) in a later year would remain exempt from action so long as those measures in the given year comply with the conditions in Article 13(b)(ii). This conclusion flows from the text of the Peace Clause (measures must conform to Article 6, and Members’ final bound commitment levels are expressed in yearly terms) as well as the nature of the subsidies challenged by Brazil (recurring subsidies that are provided yearly and expensed in the year given). For further explanation of the US interpretation of Article 13(b), please see the US answers to Questions 33 and 35 from the Panel.

81. How does the United States respond to the following in Brazil's oral statement: USA

(a) paragraph 122 (rescheduled guarantees)

154. Brazil is correct to assert “debt rescheduling does not involve any reduction in the value of outstanding debt”. A rescheduling does not involve debt forgiveness. As reflected in the terms of the various rescheduling agreements, outstanding interest is capitalized, and interest accrues on such capitalized interest as well as on outstanding principal. Further, the United States expects to recover in full pursuant to such rescheduling.

155. Therefore, from an accounting perspective, rescheduled amounts are counted as *receivables*, not losses, and are reflected as such in paragraph 173 of the US First Written Submission. Contrary to the assertion of Brazil, the United States does in fact collect on the rescheduling. The history of rescheduled Commodity Credit Corporation (CCC) export credit guarantee claims over the long-term (the 10-year period 1993-2002) confirms this position. All rescheduled claims are currently performing. In other words, all payments due up to this point under these agreements have been received.

⁸⁰With the exception of Agriculture Agreement Article 9.2(b), which is no longer applicable.

(c) paragraphs 125 ff. (guaranteed loan subsidy)⁸¹

156. The Credit Reform Act of 1990 establishes the procedures and parameters for US credit and credit guarantee programmes. In accordance with the provisions of that Act, the budgeting and accounting for US credit programmes, including the CCC export credit guarantee programmes, are based on the estimated lifetime costs to the Federal Government of making the credit available. In the case of credit guarantees, those costs are based on estimated payments by the Government to cover defaults and delinquencies, interest subsidies, and other requirements, and payments to the Government, including origination and other fees, penalties, and recoveries.

157. In presenting the annual budget, the subsidy costs of the programme reflect an *estimate* of the long-term costs to the Government. This estimate reflects various assumptions regarding credit risk, interest costs, and other factors that will apply over the lifetime period of the credit. At the time the budget is prepared, these costs are presented as estimates as of the date the budget is prepared – that is, they are a snapshot of the estimated costs. In fact, Brazil acknowledges in paragraph 125 of its oral statement that the "guaranteed loan subsidy" entry in the annual US budget is an estimate of the cost of the guarantees projected to be issued.

158. A fundamental tenet of credit reform accounting is the requirement that the performance of the credit be tracked over its lifetime. This is accomplished by tracking each cohort of credit until the credit period has expired or lapsed. A cohort consists of all transactions associated with each type of guarantee issued during a particular year – for example, all guarantees issued during fiscal year 2002 comprise a distinct cohort.

159. Activity (disbursement, repayment, claims, etc.) occurs within a given cohort over the life of all guarantees that were disbursed against that cohort. To view the data and activity strictly on an annual basis and not by cohort limits the utility of the data and distorts the costs of the programme. Not until the cohort is closed can one make an assessment as to whether or not that particular cohort represents a cost to the Federal Government.

160. All cohorts for the CCC export credit guarantee programmes under credit reform are still open although cohorts for 1994 and 1995 should close this year. At present, the 1994 cohort has a total net downward subsidy re-estimate of \$116 million. The original subsidy cost estimate for the 1994 programme was \$123 million; thus, applying the downward re-estimate, the net cost of the programme to the US Government is currently projected at \$7 million. The 1995 cohort has a total net downward subsidy re-estimate of \$149 million, versus an original subsidy estimate of \$113 million. Thus, the net cost of the 1995 programme is a receipt of \$36 million to the US Government. For 1994 and 1995 together, the total net receipt to the US Government is \$29 million.

161. The experience of 1994 and 1995 is viewed as representative of the costs of the CCC export credit programmes generally, and it is expected that, once the cohorts for other years of credit activity are closed, they will follow closely the experience of the 1994 and 1995 programmes.

(d) paragraphs 127-129 (re-estimates, etc.)

162. As discussed in response to Question 81(c), it is necessary to understand the difference between activity that occurs on a fiscal year basis as opposed to the estimates and re-estimates of subsidy that calculate net present value over the life of the programme. Although estimates and re-estimates are made annually for each cohort, these include both actual data to date and estimates of future activity for the remainder of the life of the cohort.

⁸¹The US answer to Question 81(b) follows the answer 81(d), which discusses budget re-estimates.

163. With the exception of 2002, all cohorts for annual export credit programming since the inception of credit reform accounting in 1992, have a cumulative downward re-estimate. The net total for all cohorts for guarantees issued since 1992 currently stands at a downward re-estimate of \$1.9 billion. This experience with re-estimates indicates that performance under the programme has been better than originally projected and that the original cost estimates for those programming years as presented in the annual US budget were too high. This experience also demonstrates that the assertion by Brazil at paragraph 129 of its oral statement that the original estimate of "guaranteed loan subsidy" line in the budget is an "ideal basis" for determining the costs of the programme is in error. Those estimates will be re-estimated on an annual basis until each cohort is closed and, as demonstrated above, to date the re-estimates for each cohort on a net basis have been almost exclusively downward.

(b) paragraph 123 (interest on debt to Treasury)

164. Under the guidelines for credit reform budgeting as established in the Credit Reform Act of 1990, there are two kinds of interest calculations that affect the CCC export guarantee programmes. These calculations are "snapshots" in time and will change annually for a cohort until the cohort has closed. Therefore, any one number shown in the budget for a given year is an estimate. The actual cost of the programme can be determined only when all financial activity for the cohort is completed.

165. An interest rate re-estimate is a component of the annual re-estimates of a cohort, which are made for as long as the guarantees are outstanding. The interest rate re-estimate calculates the difference between the estimated interest at the time the guarantee programme was budgeted and the actual interest at the time the guarantee is disbursed. If the actual interest is higher, the additional cost is shown in the programme account as a re-estimate. It should be noted that this cost would change with subsequent re-estimates in future years depending on the timing of the guarantee disbursement.

166. Interest on borrowings occurs in the financing account only if additional funds beyond those budgeted for a cohort is needed to pay claims. Again, these costs will vary from year to year as borrowings with a particular cohort change and the interest rate varies.

167. It is important to understand that should any interest on borrowings occur, they would be fully reflected in the costs attributed to the individual cohort. Thus, as the costs of the cohort are adjusted during the period it is active, any costs associated with the interest on borrowings are fully reflected in the programme costs. It is, therefore, incorrect to state as Brazil asserts in paragraph 123 that those payments are not fully reflected in the operating costs of the CCC export credit guarantee programmes.

(e) Exhibits BRA-125-127

168. Exhibits BRA-125-127 are pages from the Budget Estimates for the United States Government for fiscal years 1994, 1995, and 2004. These particular pages show one aspect of the budgeting for the CCC export credit guarantee programmes, the Export Loans Programme Account. In and of themselves, they do not reflect all aspects of the budgeting and financing transactions for the programmes. For example, Exhibit 127 for the fiscal year 2004 budget estimates excludes the Export Guarantee Financing Account, which appears on the following page. The data presented in the financing account is important because it presents information on both downward and upward re-estimates for the programme.

- (f) **the chart on page 53 of Brazil's oral statement at the first session of the first Panel meeting relating to "Guaranteed Loan Subsidy and Administrative Expenses of US Export Credit Guarantee Programmes GSM-102 GSM 103 and SCGP"?**

169. The table on page 53 of Brazil's oral statement at the first panel meeting presents information on budget estimates for the CCC export credit programmes for fiscal years 1992 through 2004. The data presented in the table are correct. However, as discussed previously in the answers to questions 81(c) and 81(d) above, the "guaranteed loan subsidy" is a snapshot estimate of the lifetime costs of the guarantees issued during the course of a given fiscal year. As the cohorts for those guarantees are reviewed annually over their lifetime, those estimates will change and, until the cohorts are closed out, the estimated costs of the programmes are simply that, estimates. Accordingly, Brazil is incorrect in asserting in paragraph 132 of its oral statement that, because the guaranteed loan subsidy line of the annual budget has always reflected a positive net present value, that fact indicates the programmes are "extending a subsidy to borrowers". That statement misinterprets and misrepresents the information presented in the budget.

170. In addition, Brazil makes a statement in paragraph 131 of its oral presentation with regard to the table on page 53 that likewise is incorrect. Brazil asserts that the column heading in the budget for the last completed fiscal year represents "actual" costs for the programme for that particular year. In fact, the numbers appearing in that column simply represent the latest, revised *estimate* of the costs of the programme for the fiscal year just completed. The estimate of those costs will change over the lifetime of the credit as the cohort for that year is tracked. The term "actual" is used in the column because the revised estimate is based on an actual level of guarantees issued by CCC during the year just completed.

171. Frequently, the level of guarantees issued by CCC in any given year is less than the level projected in the original budget for that year. In the case of the 2002 budget that was released in February 2001, it projected that \$3.9 billion of guarantees would be issued by CCC during that year. However, only \$3.4 billion of guarantees were actually issued. Thus, the estimate of programme costs in 2002 column of the 2004 budget has been revised to reflect that actual level of activity. Nevertheless, the cost presented in the column remains an estimate, and the estimate will continue to be revised as long as the cohort for 2002 remains active.

172. With respect to the "administrative expenses" that are displayed in the table on page 53 of Brazil's oral statement, the United States has noted elsewhere that those are imputed costs ascribed to the operation of the CCC export credit programmes as a whole.

- (g) **In respect of (a)-(f) above, how and to what extent do the information and data presented for the export guarantee programmes concerning "programme" and "financing", "summary of loan levels", "subsidy budget authority", "outlay levels", etc., in particular in Exhibits BRA-125-127, reflect "actual costs and losses" of the GSM-102, GSM-102 and SCGP export credit guarantee programmes (see e.g. Brazil's closing oral statement at the first session of the first substantive meeting, paragraph 24)? USA**

173. The closing oral statement of Brazil at the first session of the first substantive meeting of the Panel, and paragraph 24 in particular, display a fundamental misunderstanding of the budget and accounting for the CCC export credit programmes. Contrary to what is asserted in that paragraph, the information presented in the annual budget of the United States does in fact represent estimates of the lifetime costs of the programmes. Those estimates are being revised annually to reflect actual performance and, until the cohorts for the annual programmes have been closed out, the actual costs cannot be determined definitively. However, as demonstrated in response to Question 81(d), the

re-estimates thus far have resulted in a net reduction in the estimated costs of these programmes of over \$1.9 billion since the inception of credit reform budgeting in fiscal year 1992.

174. Further, as discussed in response to Question 81(c), the combined net costs of the cohorts associated with the 1994 and 1995 guarantee programmes, which are expected to close this year, are a receipt of \$29 million to the Federal Government. Based on those results, the Brazilian claim in paragraph 24 that "operating costs and losses for GSM 102, GSM 103, and SCGP have outpaced premiums collected in every single year since the United States started applying the formula in 1992" is not supportable.

82. Please explain each of the following statements and any possible significance it may have in respect of Brazil's claims about GSM-102 and GSM-103 (7 CFR 1493.10(a)(2), Exhibit BRA-38): BRA, USA

- (a) **"The programmes operate in cases where credit is necessary to increase or maintain US exports to a foreign market and where US financial institutions would be unwilling to provide financing without CCC's guarantee. (7 CFR 1493.10(a)(2), Exhibit BRA-38)**

175. The export credit guarantee programmes are generally made available in connection with middle-tier economies in which liquidity is constricted. In such cases, cash sales for all suppliers are not occurring readily. US financial institutions may face requirements regarding loan-loss reserves that impede their ability to lend.

- (b) **"The programmes are operated in a manner intended not to interfere with markets for cash sales. The programmes are targeted toward those countries where the guarantee is necessary to secure financing of the exports but which have sufficient financial strength so that foreign exchange will be available for scheduled payments." (7 CFR 1493.10(a)(2) Exhibit BRA-38)**

176. The export credit guarantee programmes are intended to operate and indeed are applied in a manner not to displace cash sales. As liquidity improves in certain countries, the use of the programme recedes. This explains, in part, the dramatic reduction in US export credit guarantees since the years immediately preceding the inception of the WTO Agreement.

177. The following table shows the dollar value of guarantees provided by the United States in US fiscal years 1992-1994, along with the average value of guarantees for fiscal years 1995 - 2002:

Fiscal Year(s)	Guarantee Value (Millions of USD)
1992	\$5,671.8
1993	\$3,853.7
1994	\$3,177.4
1995 - 2002	\$3,061.9

- (c) **"In providing this credit guarantee facility, CCC seeks to expand market opportunities for US agricultural exporters and assist long-term market**

development for US agricultural commodities." (7 CFR 1493.10(a)(2) Exhibit BRA-38)

178. Although the goal of the export credit guarantee programmes is to expand market opportunities, such goal alone has no bearing on the proper characterization of the programmes, the measures in dispute, or the conformity of the application of such programmes with the WTO obligations of the United States. Moreover, the United States is statutorily compelled to be mindful not to provide any such guarantees in connection with any country that the Secretary of Agriculture determines cannot adequately service the debt associated with such sales, nor does the United States provide guarantees in connection with any foreign bank that it has not approved and with respect to which it has not established an exposure limit.

84. Is the Panel correct in understanding that, under the GSM-102 and GSM-103 programmes, the exporter pays a fee calculated on the dollar amount guaranteed, based on a schedule of rates applicable to different credit periods? How and on what basis are the fee rates fixed? Do the fee rates ever change? If so, how and for what reason? Would it be necessary to amend the legislation and/or regulations in order to adjust the fee rates? USA

179. Fees paid by an exporter participating in either the GSM-102 or GSM-103 programme vary by the guaranteed dollar value of the transaction, the repayment period, and the principal repayment interval (annual or semi-annual). A schedule of current fees is attached as Exhibit US-20. Section 211(b)(2) of the Agricultural Trade Act of 1978, 7 U.S.C. 5641(b)(2), limits the origination fee in connection with transactions under the GSM-102 programme, except for those transactions under the CCC Facility Guarantee Programme, to no more than 1 per cent of the amount of credit to be guaranteed. There is no other legislation or regulation addressing the specific fee rates.

180. Other than the legislative restriction noted above, the CCC sets and changes the fee rates as it deems appropriate. Fee rates are changed via a press announcement to the public. The most recent change in guarantee fee rates occurred on 1 October 2002, at which time the fee schedule was modified to include rates for transactions with 30- and 60-day repayment periods. Previously, the fee schedule had been adjusted to accommodate variable interest rates as opposed to fixed rates. Legislative amendment is not required to change the fee rates unless the rates for the GSM-102 programme are to exceed 1 per cent of the guaranteed dollar value of a transaction. Neither is it necessary to amend the programme regulations in order to change the fee rates.

85. Is the Panel correct in understanding that, under the SCGP, the exporter pays a fee for the guarantee calculated on the guaranteed portion of the value of the export sales? How and on what basis are the fee rates fixed? Do the fee rates ever change? If so, how and for what reason? Would it be necessary to amend the legislation and/or regulations in order to adjust the fee rates? Please explain any "risk" assessment involved in the programme. USA

181. Under the SCGP, the exporter pays a fee to CCC based on the guaranteed dollar value of the export transaction and the repayment period. The current guarantee fee rates are \$0.45 per \$100 of coverage for credit terms up to 90 days, and \$0.90 per \$100 of coverage for credit terms up to 180 days. Section 211(b)(2) of the Agricultural Trade Act of 1978, 7 U.S.C. 5641(b)(2), limits the origination fee in connection with transactions under the SCGP to no more than 1 per cent of the amount of credit to be guaranteed. There is no other legislation or regulation addressing the specific fee rates.

182. Other than the legislative restriction noted above, the CCC sets and changes the fee rates as it deems appropriate. For example, fee rates for the SCGP were changed in US fiscal year 2000 (beginning 1 October 1999) and set at their current level. Prior to that time, the fee rate was \$0.95 per

\$100 of coverage regardless of the repayment period. The fee rates were changed to give exporters and importers an incentive to negotiate repayment terms of less than 180 days. Legislative amendment is not required to change the fee rates unless the rates for the SCGP are to exceed 1 per cent of the guaranteed dollar value of a transaction. It is not necessary to amend the programme regulations in order to change the fee rates.

183. CCC carries out a country risk assessment for each country prior to announcing its eligibility for SCGP participation. Country risk assessment entails a review of the economic and political situation in each country to ensure there is a reasonable expectation that the country's importers will be able to repay debts incurred under the programme. CCC does not determine the creditworthiness of importers participating in the SCGP. CCC provides a guarantee covering 65 per cent of the export transactions under the programme; the exporter or his assignee (US bank) must accept the remaining 35 per cent of the transaction's risk. This "risk sharing" between CCC and the exporter/assignee is intended to ensure that due diligence is performed in assessing an importer's creditworthiness before undertaking a transaction with that importer.

86. Is there a risk categorization in relation to three export credit guarantee programmes (GSM-102, GSM-103 and SCGP)? Does this have any impact on premiums payable and the ability of the CCC to on-sell the guarantees ? USA

184. All countries eligible for any of the CCC export credit guarantee programmes are categorized according to risk. CCC categorization of countries is based on a US government internal risk classification system. This system is administratively controlled and may not be released outside of the US Government. A country's risk classification has no impact on the premiums payable under the US export credit guarantee programmes. There is no secondary market for CCC guarantees; therefore, CCC does not "on-sell" the guarantees.

87. What proportion of CCC (export-related and total) long term operating costs and losses are represented by GSM-102, GSM-103 and SCGP programmes? USA

185. With the advent of the Credit Reform Act, the export guarantee programmes are not financed out of the Commodity Credit Corporation. While the programmes continue to be run through the authorities and facilities of the CCC, all budget authority (funding) for the guarantee programmes is provided directly to accounts for those programmes from the US Treasury.

88. (a) Is the Panel correct in understanding that the United States' argument is that, at present, by virtue of Article 10.2 of the Agreement on Agriculture, there are no disciplines on agricultural export credit guarantees under the Agreement on Agriculture (or the SCM Agreement)? USA

186. Article 10.2 provides: "Members undertake to work toward the development of internationally agreed disciplines to govern the provision of export credits, export credit guarantees or insurance programmes and, after agreement on such disciplines to provide export credits, export credit guarantees or insurance programmes only in conformity therewith." Article 10.2 imposes an obligation on Members to work toward "internationally agreed disciplines" and, upon agreement on such disciplines, to provide export credit guarantees only in conformity with such disciplines. This was the purpose of the negotiations in the OECD that followed the Uruguay Round, and which now are occurring under the aegis of the WTO. If and when such disciplines are agreed upon, they are WTO obligations under the Agreement on Agriculture.⁸²

⁸²This is similar to other work programs that continued beyond the close of the Uruguay Round. See US First Written Submission, paras. 154-66.

187. Brazil's argument is that such "internationally agreed disciplines" already apply. If export credit guarantee programmes were already subject to export subsidy disciplines, then Article 10.2 would be unnecessary. That is, Members would *already* have "to provide . . . export credit guarantees . . . only in conformity" with the internationally agreed disciplines of the WTO. In Brazil's oral statement, Brazil attempts to avoid this implication of its reading by repeatedly attempting to insert the word "specific" into the text of Article 10.2 – that is, "undertake to work toward the development of *specific* internationally agreed disciplines . . ."⁸³ That word is not there, however. The United States' interpretation of Article 10.2 gives meaning to the text of Article 10.2 as drafted and agreed by Members whereas Brazil's reading would effectively read it out of the Agreement on Agriculture.

- (b) **Does the United States agree with the following proposition: a WTO Member may therefore extend agricultural export credit guarantees without charging a premium, and for an indefinite period, in addition to any other terms and conditions it may wish? How would this reconcile with the title of Article 10 of the Agreement on Agriculture ("Prevention of Circumvention on Export Subsidy Commitments"), and with other commitments contained in the Agreement on Agriculture? Please cite any relevant material, including any past WTO dispute settlement cases. How would this reconcile with the United States' own statement, at paragraph 21 of its closing oral statement that "of course, the United States may not provide subsidies without any limit". USA**

188. Article 10.2 applies only to export credit guarantees (and export credits and insurance programmes) properly characterized as such. In the case of the United States, export credit guarantees are offered pursuant to programmes which charge premiums; impose limits on tenor; impose limits on exposure to individual bank obligations; impose limits on exposure to risk of default from different countries; define shipping periods; and issue allocations (value limitations) of potential guarantee availability for specific commodities to be exported to specific destinations. The United States also guarantees only a relatively small portion of interest. Consequently, participants remain exposed to a significant component of the over-all risk of default.

189. The United States submits that the deferral of disciplines under Article 10.2 properly applies to export credit guarantees offered pursuant to a programme with such characteristics; indeed, Brazil has not contested that US export credit guarantee programmes are encompassed by the terms of Article 10.2. Illegitimate attempts to characterize export subsidy programmes as export credit guarantee programmes would be subject to the anti-circumvention provisions of Article 10.1 and the other commitments of the Agreement on Agriculture.⁸⁴

190. The US interpretation of Article 10.2 presents no conflict with the title of Article 10, which provides relevant context in interpreting the provisions of Article 10. Article 10 is entitled "Prevention of Circumvention on Export Subsidy Commitments." Article 10.2 contributes to the prevention of circumvention of export subsidy commitments by imposing two obligations on Members: first, they must undertake to work toward the development of internally agreed disciplines

⁸³See, e.g., Brazil's Oral Statement, para. 100 ("Article 10.2 instead announces Members' intent to work toward negotiations on *specific* disciplines for export credits.") (italics in original); *id.* ("In the meantime, while those *specific* disciplines are being discussed . . .") (emphasis added); *id.*, para. 102 ("Under the first part of Article 10.2, therefore, WTO Members have pledged to work toward the development of *specific* disciplines . . .") (emphasis added); *id.*, para. 103 ("If Members do conclude an agreement on these *specific* disciplines . . .") (emphasis added); *id.* (Brazil and the United States agree that there has been no agreement on any such *specific* disciplines . . .") (emphasis added).

⁸⁴For example, the United States could not simply change the name of the FSC Repeal and Extraterritorial Income Exclusion Act to the "FSC Repeal and Extraterritorial Income Exclusion Export Credit Guarantee Program" and successfully assert that the deferral of disciplines contemplated by Article 10.2 applies to such re-named program.

on export credit guarantees; second, “after agreement on such disciplines,” they must provide export credit guarantees “only in conformity therewith”. Thus, Members agreed that those internationally agreed disciplines would constrain the provision of export credit guarantees, which in turn would contribute to the goal of Article 10, to prevent the circumvention of export subsidy commitments.

191. Although the language quoted from paragraph 21 of the United States' closing oral statement was intended to address concerns involving domestic support for upland cotton,⁸⁵ it also applies in the case of export subsidies. The United States also cannot provide export subsidies without limit. It has a schedule of export subsidy reduction commitments for 12 commodities. For these commodities, export subsidies can only be provided in accordance with such schedule. For the remainder of agricultural commodities, the United States cannot provide export subsidies at all.

192. Although internationally agreed disciplines on export credit guarantee programmes have yet to be agreed, the characteristics of such programmes and the discipline inherent in the risk-sharing aspects of such programmes impose an internal constraint on their use. Indeed, the use of US export credit guarantee programmes has *declined* since the period before the inception of Uruguay Round commitments. As shown in the US answer to Question 82(b), the dollar value of guarantees provided by the United States in US fiscal year 1992 was \$5,671.8 million, in fiscal year 1993 was \$3,853.7 million, and in fiscal year 1994 was \$3,177.4 million. In contrast, the average value of guarantees for fiscal years 1995 - 2002 was only \$3,061.9 million. Any concerns about unchecked use of export credit guarantee programmes, then, are not supported by the post-Uruguay Round experience.

- (c) **If, as the United States argues, there are no disciplines on export credit guarantees in the Agreement on Agriculture, how could export credit guarantees "conform fully to the provisions of Part V" of the Agreement on Agriculture within the meaning of Article 13 (how can you assess "conformity" or non-conformity when there are allegedly no disciplines against which such an assessment could occur)? USA**

193. US export credit guarantee programmes provide “export credit guarantees” within the meaning of Article 10.2 and therefore will be subject to disciplines only as contemplated by that Article. Because no such disciplines currently exist, these programmes cannot be out of compliance with Part V of the Agriculture Agreement. Moreover, export credit guarantees are not export subsidies within the meaning of either Article 9.1 or 10.1, and since they are not export subsidies, Article 13(c) does not apply to them.

- (d) **Is the United States advocating the view that its own export credit guarantee programmes, which pre-dated the Uruguay Round, are effectively "grandfathered" so as to benefit from some sort of exemption from the export subsidy disciplines of the Agreement on Agriculture? How, if at all, is it relevant that the SCGP did not, according to the United States, become relevant for upland cotton until the late 1990's (i.e. after the entry into force of the WTO Agreement)? USA**

194. It is not entirely clear what is meant by the term “grandfathering” in this connection. Agriculture Agreement Article 10.2 defers the imposition of disciplines on export credits, export

⁸⁵The statement itself was intended to note that the United States is subject to the limit set forth in its domestic support reduction commitments for the Current Total Aggregate Measurement of Support. This amount, across all US commodities, is \$19.1 billion. In addition, a very specific limit applies with respect to domestic support for upland cotton under the Peace Clause. It may not exceed the rate of 72.9 cents per pound, as decided in 1992, without removing the Peace Clause protection of Article 13 of the Agreement of Agriculture.

credit guarantees, and insurance programmes until internationally agreed disciplines are reached, and in that sense the export subsidy disciplines of the Agreement do not apply to the export credit guarantee programmes at issue in this dispute.

195. The SCGP began in 1996, and no transactions occurred under this programme in connection with cotton until fiscal year 1998, which began in September 1997. Although the negotiators obviously could not have considered the application of this specific programme, it is substantially similar in its operation to other US export credit guarantee programmes. Again, Brazil has not contested that SCGP provides export credit guarantees within the meaning of Article 10.2. Thus, the deferral of disciplines under Article 10.2 similarly applies.

STEP 2 PAYMENTS

89. Does the United States confirm Brazil's statement in paragraph 331 of its first submission that "The conditions and requirements for Step 2 domestic payments remain unchanged with the passage of the 2002 FSRI Act"? What is the relevance of this, if any, to this dispute? USA

196. While the Step 2 programme under the 2002 Act is largely consistent with the programme under the 1996 Act, there have been some modifications since the inception of the programme, relating to the precise nature of the price differential formula and the price ceiling for the Step 2 payments. The 2002 programme was unchanged from the 1996 Act programme, as amended, except for suspending the 1.25 cent differential. In the end, this is inconsequential because it does not materially affect the levels of support decided in marketing year 1992 (72.9 cents per pound) or that measures currently grant (52 cents per pound).

90. Does the United States confirm Brazil's statement in paragraph 235 of its first submission that the changes concerning Step 2 export payments from the 1996 FAIR Act to the 2002 FSRI Act are: increase in the amount of the subsidy by 1.25 cents per pound and the removal of any budgetary limits that applied under the 1996 FAIR Act? What is the relevance of this, if any, to this dispute? USA

197. As noted in the US answer to Question 89, the 2002 Act suspended the 1.25 cents differential, but the United States disagrees with the assertion of increased budgetary exposure for the programme. First, we note that Step 2 for the 1992 crop and marketing years was covered by the provisions of the 1990 Act, which had no limit on the amount of expense that could be undertaken in Step 2. For the 1996 Act, which covered the 1996-2002 crops until supplanted by the 2002 Act, there was a limit of \$701 million for the six-year duration of the Act, and in fact that money did run out in December 1998. However, the Congress removed the budgetary limit of the 1996 Act as of October 1999 (Public Law No. 106-78, 22 Oct. 1999). Therefore, neither the 2002 Act, nor the 1996 Act (as of October 1999), nor the 1990 Act had budgetary limits on Step 2 expenditures.

198. While the potential step 2 payment (when price conditions in the statute are met) is higher in the 2002 Act than under the 1996 Act by as much as (but not more than) 1.25 cents per pound, step 2 merely changes the vehicle of support.

91. What is the significance of the elimination of the 1.25 cent threshold payment in the 2002 FSRI Act pertaining to Step 2 payments? USA

199. Please see the US answers to Question 89, 90, and 117.

92. Does the United States confirm that Exhibit BRA-65 represents a sample contract for exporters of eligible upland cotton to conclude with the CCC under the FSRI 2002, and that an application form (Exhibit BRA-66) needs to be filled out with data on weekly

exports and submitted to the USDA FAS. Is Exhibit BRA-66 - Form CCC 1045-2 - also a valid example? If not, please identify any differences or distinctions. USA

200. The Brazilian exhibits appear to be accurate versions of old Step 2 programme documents. Some of the documents in the exhibit are for domestic handlers and involved programme payment assignments. We also note that, in making an export claim, other documentation like bills of lading may be needed.

201. The official documents for the upland cotton step 2 programme can be found at the Farm Services Agency website (www.fsa.usda.gov/daco, click on "cotton" and on "upland cotton user marketing certificate programme".) There is a common contract that exists for both domestic users and exports under the Step 2 programme, CCC Form CCC-1045UP. Because of the different nature of uses and therefore applications, there are separate reporting forms: CCC-1045UP-1 for domestic users and CCC-1045UP-2 for Exporter Users. Recently updated documents used for this programme are attached as Exhibit US-21.

93. Please elaborate why the United States deems that Step 2 payments upon submission of proof of export are not subsidies contingent upon export. Is it the US contention that, in order to be contingent on export, exportation must be the exclusive condition for receipt of the payment? USA

202. As the United States has indicated, all upland cotton produced in the United States is eligible for the benefit of the Step 2 cotton subsidy. If the statutory price condition applies, all US upland cotton used during the applicable period of time will receive the subsidy. "Use" in domestic manufacture or export constitutes the universe of potential use of US upland cotton. The United States submits that when the entirety of production of a good in a country is eligible to receive a subsidy, no contingency on export exists. The Step 2 subsidy is entirely distinct in this regard from a hypothetical situation in which a subsidy is theoretically available for domestic use, but in reality is exclusively or nearly exclusively available in connection with exports.

95. Do the criteria in 7 CFR 1427.103(c)(2) (Exhibit BRA-37) that Step 2 "eligible upland cotton" must be "not imported cotton" apply to both domestic and export payments? USA

203. Only domestic cotton is eligible for Step 2 payment, which is made if the statutory price conditions are met and requisite proof of use is submitted.

96. Is a domestic sale a "use" for the purposes of Step 2 payments? Is a sale for export, or export, considered a "use"? USA

204. A sale is not a use for purposes of the Step 2 subsidy. For domestic manufacture, opening the cotton bale constitutes use. For exports, similarly, the sale alone does not itself constitute use; the exporter must demonstrate actual exportation.⁸⁶

97. How does the United States respond to Brazil's assertion, at paragraph 70 of Brazil's oral statement at the first session of the first substantive meeting, that "It is obvious that a single bale of cotton cannot be both exported and used domestically." Is this a relevant consideration? USA

205. It is unclear what Brazil's assertion is intended to demonstrate. The Step 2 programme makes payments to documented users of US upland cotton. If a bale cannot be both opened domestically and exported (although it is not clear why that would be so), that amounts to arguing that a single bale

⁸⁶7 Code of Federal Regulations 1427.103(a).

cannot be “used” twice. The fact remains that *either* opening the bale domestically *or* exporting it – that is, the universe of activities resulting in use of US upland cotton – is entitled (given certain market conditions) to a Step 2 payment.

206. The United States notes, moreover, that it may actually be possible (economic realities aside) that the same bale could be exported and then brought back into the country and opened for domestic use. (Please see the US answer to Question 98 for more detail.) The US Department of Agriculture’s position would be that the payment should be made on the bale once only. The purpose of the programme is to provide support to upland cotton farmers. Once the bale has been purchased by an upland cotton user, there would be no additional support for upland cotton farmers from providing Step 2 payments on additional “uses” of the same bale.

98. How many Step 2 payments are received if a bale of upland cotton is exported, and then opened by a domestic user in the United States, or vice versa? USA

207. If a bale were exported and then imported and opened up (or vice versa) it would be the US position that only one payment would be made. It does not appear that this situation has ever arisen in fact, but we note that the Step 2 regulations specifically provide that “imported” cotton is not eligible for payment. Such cotton may include any cotton that was imported, even if it had been produced in the United States.

99. How does the United States respond to Brazil's arguments in paragraphs 71-75 of Brazil's oral statement at the first session of the first Panel meeting concerning the relevance of the Appellate Body Report in US-FSC (21.5). USA

208. In contrast to the facts of the *United States – FSC (21.5)* dispute, in this dispute all of the product is produced in the United States; all of the product is eligible to receive the benefit of the subsidy; and all of the potential uses of the product are similarly eligible. If the statutory formula of price conditions applies, all US upland cotton used during that time – regardless of how such use is manifested – will receive the subsidy. This case involves only one factual situation: use of cotton during a particular period of time. The only factual distinction applicable here is whether the applicable price conditions are on or off. Brazil's emphasis on the “different instructions” in the programme regulations is misplaced. Such instructions are simply to demonstrate the requisite use and to assure payment is made to the proper party. If upland cotton could be used in a third or fourth way, this would not change the eligibility for subsidy but would necessitate a parallel third or fourth set of instructions to demonstrate that form of use as well.

103. Is the Step 2 programme fund a unified fund that is available for either domestic users or exporters, without a specific amount earmarked for either domestic users or exporters? Please substantiate your response, including by reference to any applicable statutory or regulatory provisions. USA

209. The upland cotton user marketing certificate programme (Step 2) makes no differentiation between funds for payments to exporters and domestic handlers – it is all one programme. The first paragraph of the Step 2 rule states:

These regulations set forth the terms and conditions under which CCC shall make payments, in the form of commodity certificates or cash, to eligible domestic users and exporters of upland cotton who entered into an Upland Cotton Domestic User/Exporter Agreement with CCC to participate in the upland cotton user marketing certificate

The Step 2 rule was published on 18 October 2002, at 67 Federal Register 64454, and is codified at 7 Code of Federal Regulations 1427.100-.108.

210. As with other US domestic support measures, Step 2 payments are funded through the Commodity Credit Corporation, which has a borrowing authority in the Treasury and as such does not rely on appropriations. This is provided for in Sections 1207 and 1601(a) of the 2002 Act and codified at 7 US Code 7937 and 7991.

104. How does the United States respond to the data presented in Exhibit BRA-69? Is it accurate? Please substantiate. USA

211. The data in Exhibit BRA-69 is not official US Government data, and Brazil has not indicated the source of the information. Thus, we cannot confirm its reliability. The United States has tried in any event to obtain information in the format of Bra-69, which is not maintained and published by the US Government in that manner. The following data has been collected by the US Department of Agriculture and attempts to designate (as in Bra-69) Step 2 payments by fiscal year⁸⁷ and use.

User Marketing Certificate (Step 2) Payments, by Fiscal Year and Use		
Fiscal Year	Mill Use (US \$)	Export Use (US \$)
1991	4,311,991	17,259
1992	102,769,543	30,852,107
1993	113,401,813	89,095,640
1994	28,251,613	178,266,742
1995	17,571,224	75,200,203
1996	0	34,798,579
1997	6,201,540	2,875,936
1998	255,502,154	158,924,004
1999	165,831,362	113,521,476
2000	260,075,318	185,273,956
2001	144,849,807	90,903,021
2002	72,425,112	105,415,152

A comparison with Exhibit BRA-69 suggests that the Brazilian data is inaccurate.

212. During the first panel meeting, the Panel asked about the figures shown for fiscal year 1996, which showed a zero payment for mill use and a positive number for export use. We suggested that perhaps appropriated amounts had suddenly run out, but our suggestion was not accurate. Rather, the odd numbers for fiscal year 1996 resulted because, at the time, payments for export use accrued when the contract for export was made. However, such payments were not paid until the export actually took place, at which time the exporter would be paid based on the Step 2 rates that applied when the

⁸⁷The US fiscal year runs from October 1 - September 30, such that the 2002 fiscal year would run from 1 October 2001, through 30 September 2002.

contract was made. As the Panel is aware, Step 2 payments can be made only when there is a difference between world and US prices for cotton for a certain time period. In the case of fiscal year 1996, these prices did not satisfy the Step 2 conditions, but there were some payments that were made during that fiscal year because they had accrued by an export contract made in the previous fiscal year. That rule is now changed⁸⁸ so that the rate that applies for export use is the rate that is in effect when the export is made not when the contract for export was made.

105. Why is the Step 2 programme separated into "domestic users" and "exporters"? Apart from differentiating between exporters and domestic users, with consequential differentiation as to the forms that must be filled out and certain other conditions that must be fulfilled, are the eligibility criteria for Step 2 payments identical? Are the form and rate of payment, as well as the actual payment made, identical? USA

213. US law does not separate the Step 2 programme into domestic users and exporters. There is but one Step 2 statute – codified at 7 US Code 7937 – and but one Step 2 rule for all users – found at 7 Code of Federal Regulations 1427.100-108. The statute and rule do identify “domestic users” and “exporters” as the universe of *bona fide* users of upland cotton and thus potential recipients for Step 2 payments. Therefore, the only distinction drawn between these recipients is the proof of use: domestic handlers are paid when they open a bale, and exporters are paid when they export. The form and rate of payment are identical.

106. With respect to paragraph 139 of the United States' first written submission, are Step 2 export payments included in the annual reduction commitments of the United States? If so, why? USA

214. The United States does not distinguish between the uses of US upland cotton for purposes of reporting the subsidy because the subsidy is not contingent on export performance. All Step 2 payments are reported as product-specific domestic support for upland cotton and are included within the Total Aggregate Measurement of Support calculation for purposes of *domestic support* reduction commitments.

107. Please comment on any relevance, to Brazil's de jure claims of inconsistency with the provisions of the Agreement on Agriculture, of Exhibit BRA-69, which shows Step 2 payments made to (i) domestic users and (ii) exporters. This Exhibit shows that, from FY 91/92 through 02, the Step 2 payments for exporters exceeded those for domestic users in FY 94; FY 95; FY 96 (in fact there were no domestic payments in FY 96); and FY 02. In the other years, the domestic payments are greater than export payments. BRA, USA

215. Without commenting on the accuracy of the specific numbers set forth in Exhibit BRA-69, it is entirely possible that in certain years one type of user happened to receive a larger share of payments than another type of user. This would entirely be a function of market conditions and relative demand for manufacture or for export. That is, differences in amounts paid to exporters and domestic users during any time period are happenstance based on actual use of US upland cotton.

216. The United States notes that payments to exporters were previously made based on when exporters finalized the sale contract, not on when the cotton was actually exported. In the specific case of fiscal year 1996, it appears that payments for exported upland cotton *accrued* during a period when Step 2 payments were allowed by the statute, but that the payments were actually made at a time when market conditions no longer met the statutory criteria for payment. The rule has been changed,⁸⁹ and that situation can no longer recur.

⁸⁸ See 61 Federal Register 37544, 37548 (18 July 1996).

⁸⁹ See 61 Federal Register 37544, 37548 (July 18, 1996).

108. At paragraph 135 of its first written submission, the United States states : "[T]he subsidy is not contingent upon export performance..." (emphasis added). Again, in the course of the first Panel meeting, the United States admitted that the Step 2 payments were "subsidies". Does the United States thus concede that Step 2 payments constitute a "subsidy" within the meaning of the WTO Agreement? USA

217. The United States has always maintained that Step 2 payments are subsidies that provide domestic support in favour of US agricultural producers.

109. How does the United States respond to Brazil's arguments concerning a mandatory/discretionary distinction and the allegation that certain United States measures (including s.1207(a) of the 2002 FSRI Act) are mandatory? (This is referred to, for example, in paragraph 28 of Brazil's first written submission). Does the United States agree with the assertion that (subject to the availability of funds) the payment by the Secretary of Step 2 payments is mandatory under section 1207(a) FSRI upon fulfilment by a domestic user or exporter of the conditions set out in the legislation and regulations? If not, then why not? To what extent is this relevant here? What determines the "availability of funds"? Please cite any other relevant measures or provisions which you consider should guide the Panel in respect of this issue. USA

218. The United States does not disagree that, subject to the availability of funds (that is, the availability of CCC borrowing authority), Step 2 payments must be made to all those who meet the conditions for eligibility. With respect to the well-accepted mandatory/discretionary distinction reflected in GATT 1947 and WTO panel and Appellate Body reports, the United States notes that the distinction is the natural consequence of the fact that there can be no presumption of bad faith in WTO dispute settlement, a fact that numerous Members, including the European Communities, have emphasized.⁹⁰ Thus, to the extent that a Member retains discretion under a measure to act in accordance with a WTO obligation, it may not be presumed that the Member will violate that obligation, or to conclude that the measure itself – separately from the measure's application in a specific instance – may be found inconsistent with that obligation.

110. Section 1207(a) of the 2002 FSRI Act provides that during the period beginning on the date of the enactment of the FSRI Act through July 31 2008, " .. the Secretary shall issue marketing certificates or cash payments, at the option of the recipient, to domestic users and exporters for documented purchases by domestic users and sales for export by exporters...". The Panel notes that Brazil does not appear to distinguish between the treatment of (i) cash payments and (ii) marketing certificates in terms of the issue of whether or not a "subsidy" exists. The United States refers to "benefits" and "payments" and "programme" in asserting that Step 2 is not export contingent (paragraphs 127-135 of the United States' first written submission).

(a) Do the parties thus agree that there is no need to draw any distinction between the treatment of (i) cash payments and (ii) marketing certificates in terms of the issue of whether or not a "subsidy" exists for the purposes of the Agreement on Agriculture? BRA, USA

219. The United States agrees that there is no need to draw a distinction between cash payments and marketing certificates in terms of whether a subsidy exists for purposes of the Agreement on Agriculture.

⁹⁰See Appellate Body Report, *United States - Section 211 Omnibus Appropriations Act of 1998*, WT/DS176/AB/R, adopted 1 February 2002, para. 259.

(b) Why would a domestic user or an exporter select to receive a marketing certificate over a cash payment? What is the proportion of cash payments vs. marketing certificates granted under the programme? USA

220. A user of upland cotton that elects to receive payment in the form of a marketing certificate is entitled to redeem that certificate for an equivalent amount of upland cotton held by the Commodity Credit Corporation (CCC). Although authorized by statute, no Step 2 payments have been made in recent times in the form of certificates. Marketing certificates in lieu of cash payments for Step 2 were last used heavily in the early to mid-1990s. The CCC does not currently maintain high upland cotton inventories from which such certificates if issued could be redeemed.

111. Does the United States maintain its argument that actions based on Article 3.1(b) of the SCM Agreement are conditionally "exempt from actions" due to the operation of Article 13 of the Agreement on Agriculture? USA

221. Article 13(c) provides that "export subsidies that conform fully to the provisions of Part V of this Agreement, as reflected in each Member's Schedule, shall be . . . exempt from actions based on Article XVI of GATT 1994 or Articles 3, 5 and 6 of the Subsidies Agreement." Article 13(b), which applies to domestic support measures, does not reference Subsidies Agreement Article 3. Brazil has advanced claims under Article 3.1(b) of the Subsidies Agreement only with respect to Step 2 payments, which are domestic support measures and not export subsidies. Thus, on the US view the Peace Clause would not appear to be applicable; however, to the extent Brazil asserts that Step 2 payments (or some part thereof) are export subsidies, Article 13(c) would be relevant.

222. We also note that paragraph 7 of Annex 3 requires that support in favour of domestic agricultural producers that is provided through payment to processors shall be included in the AMS of the Member. If payments are made in connection with both domestic and foreign product then such payments are not support in favour of domestic agricultural producers. Consequently, the Agriculture Agreement necessarily contemplates that support paid to processors may be paid solely with respect to domestic production. Under Article 6.3 of the Agriculture Agreement, if a Member is providing support within its domestic support reduction commitments, then such support may not be challenged under Article 3.1(b) because that Article applies "[e]xcept as provided in the Agreement on Agriculture". If a Member exceeds its domestic support reduction commitments, on the other hand, then such support paid to processors would be actionable under Article 3.1(b).

112. In the event that the Panel finds that Article 6.3 of the Agreement on Agriculture does not preclude an examination of Brazil's claims under Article 3.1 of the SCM Agreement and Article III:4 of GATT 1994, how does the United States respond to the merits of Brazil's claims relating to Step 2 payments under those provisions? USA

223. As indicated in the US answer to Question 111 from the Panel, and as the European Communities has noted in its third party submission, inasmuch as paragraph 7 of Annex 3 of the Agreement on Agriculture requires support in favour of agricultural producers that is paid to processors to be included in the Member's Aggregate Measurement of Support, then the Agreement on Agriculture necessarily contemplates that such payments to processors may apply solely with respect to domestic product. Otherwise, as in the case of Step 2 payments, domestic cotton producers would not receive the relative price benefit conferred by the payment. Consequently, such discrimination in favour of domestic production is permitted under the Agreement on Agriculture and, under Article 21.1 of that Agreement, the provisions of GATT 1994 and of other Multilateral Trade Agreements in Annex 1A to the WTO Agreement are expressly "subject to the provisions of [the Agriculture] Agreement." For that reason, neither Article 3.1(b) of the Subsidies Agreement nor GATT 1994 Article III:4 precludes such payments to users of US upland cotton, unless the United States exceeds its domestic support reduction commitments.

113. Is it necessary for measures directed at agricultural processors included in AMS to discriminate on the basis of the origin of goods? USA

224. The United States does not express an opinion whether it is necessary in all circumstances for all Members with respect to all commodities. However, paragraph 7 of Annex 3 of the Agreement on Agriculture certainly contemplates that support in favour of domestic producers provided by payments to processors is included in the Aggregate Measurement of Support. In the case of Step 2 payments on upland cotton, if payments were provided in favour of all upland cotton, whether domestic or foreign, used by domestic mills or exporters, the price benefit for US producers would not be achieved. Without such a benefit to US producers, these payments would not need to be included in the Aggregate Measurement of Support. The Agreement on Agriculture does not preclude payments that solely benefit domestic producers; indeed, paragraph 7 contemplates such discriminatory subsidy payments. Accordingly, the United States reports all Step 2 payments as domestic support in favour of US producers of upland cotton.

115. What is the meaning and relevance (if any) to Brazil's claims under Article 3 of the SCM Agreement and Article III:4 of GATT 1994 of the phrase "measures directed at agricultural processors shall be included to the extent that such measures benefit the producers of the basic agricultural products" in the Agreement on Agriculture? BRA, USA

225. The United States directs the Panel's attention to the US answers to Questions 111, 112, and 113 from the Panel.

116. With respect to paragraph 32 of the oral statement of the EC, are subsidies contingent on the use of domestic goods consistent with the Agreement on Agriculture? Does the phrase "provide support in favour of domestic producers" in Article 3.2 of the Agreement on Agriculture refer to, and/or permit such subsidies? BRA, USA

226. Subsidies contingent on the use of domestic goods may be consistent with the Agreement on Agriculture. Paragraph 7 of Annex 3 of the Agreement requires the United States to include its Step 2 payments in favour of domestic upland cotton producers, even though such payments are made to processors, within its calculation of its Aggregate Measurement of Support. The United States has complied with its domestic support reduction commitments. Therefore, Step 2 payments to upland cotton users that provide support to domestic producers contingent on the use of domestic goods is consistent with the Agreement on Agriculture. If Members could not discriminate in favour of domestic producers when making subsidy payments through processors, there would be no reason for paragraph 7 of Annex 3. Such payments that are not limited to domestic products would not be in favour of domestic producers because the relative economic benefit of the subsidy vis-à-vis foreign production would not exist.

117. What is the relationship between Step 2 payments to exporters and the marketing loan payments, both of which appear to compensate for the price differences relative to the Liverpool A-Index? For example, is there double compensation? Or is one of the explanations that these export-related price compensatory payments are paid to different operators (namely, the producer, on the one hand under the marketing loan arrangements, and the processor/users (Step 2 programme) arrangements on the other? USA

227. Both marketing loan payments and Step 2 payments are domestic support for upland cotton, but the marketing loan payment is made directly to the producer whereas the Step 2 payment is made to users of the cotton. The marketing loan repayment formula, in section 1204 of the 2002 Act, and the Step 2 payment formula in section 1207 of the 2002 Act, differ by their terms and are simply

different forms of support, the latter (Step 2) being a form of support that can facilitate higher market prices for US cotton. We will address this more fully in our rebuttal submission.

118. Can the United States confirm that it does not rely on Article III:8 of GATT 1994? USA

228. The United States can confirm that the Step 2 payment is not made exclusively to domestic producers.

ETI ACT

119. How does the United States respond to Brazil's reference to the panel report in India - Patents (EC) (at paragraph 138 of its oral statement at the first session of the first substantive meeting)? How, if at all, should the Panel take this report into account in considering the issues raised by Brazil's claims relating to the ETI Act? USA

229. We agree with the passage quoted from the *India – Patents* dispute and consider it relevant to the extent that: Brazil has identified the challenged measure; Brazil has argued why the reasoning of the panels and Appellate Body are relevant in determining that the measure is inconsistent; and the Panel finds the reasoning in *FSC/ETI* persuasive. Our argument in the first written submission went to whether Brazil had carried its burden of bringing a *prima facie* case, in order to assist the Panel to fulfill its obligation under DSU Article 11 to make an objective assessment of the matter before it. Brazil may consider that it should not have to meet this burden, but under DSU rules as currently agreed, it must.⁹¹ Finally, we note our statement in the first submission that “[w]hile the United States cannot specify the precise date on which this will occur, the United States is confident that the ETI Act will be repealed in the reasonably near future.”⁹²

121. How do you respond to the reference in paragraph 43 of EC third party oral statement with respect to the relevance of Article 17.14 of the DSU, and, in particular, the phrase "a final resolution to that dispute" (emphasis added)? Please explain the use, and relevance (if any) of the term "disputes" in Articles 9.3 and 12 and Appendix 3 of the DSU, and please cite any other provisions you consider relevant. USA, BRA

230. The United States considers the EC's references to be irrelevant to the resolution of this dispute. As noted in the US first written submission, the United States intends to implement the DSB's recommendations and rulings in the *FSC/ETI* dispute. Further, the issues raised in the US first written submission related solely to whether Brazil had met its burden of argumentation in this dispute and not to the substantive correctness and applicability, or lack thereof, of the adopted findings in *FSC/ETI*. Nor did the US arguments relate to the breadth of the US obligation to implement the DSB's rulings and recommendations in that dispute. The United States considers that Brazil's burden in this dispute requires, at a minimum, that it identify those aspects of the measure which are WTO-consistent and explain why that is the case.

⁹¹See TN/DS/W/45 (Brazilian proposal in ongoing DSU review: "Brazil understands that one of the drawbacks of the current dispute settlement mechanism is the necessity for a Member to litigate a case *de novo* through all the established phases even if the same measure nullifying or impairing benefits of this Member has already been found WTO inconsistent in previous panel or appeal proceedings initiated by another Member.").

⁹²US First Written Submission, para. 189.

ANNEX I-3

COMMENTS OF BRAZIL TO ANSWERS TO QUESTIONS POSED BY THE PANEL FOLLOWING THE FIRST SUBSTANTIVE MEETING OF THE PANEL

22 August 2003

TABLE OF CONTENTS

	<u>Page</u>
I. PRELIMINARY ISSUES.....	136
II. ARTICLE 13(B): DOMESTIC SUPPORT MEASURES.....	141
A. "EXEMPT FROM ACTIONS"	141
B. "SUCH MEASURES" AND ANNEX 2 OF THE AGREEMENT ON AGRICULTURE	145
C. "DO NOT GRANT SUPPORT TO A SPECIFIC COMMODITY"	146
D. "IN EXCESS OF THAT DECIDED DURING THE 1992 MARKETING YEAR"	148
III. EXPORT CREDIT GUARANTEES.....	156
IV. STEP 2 PAYMENTS.....	166

Table of Cases Cited

Short Title	Full Case and Citation
EC – Bananas (III)	Appellate Body Report, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas</i> , WT/DS27/AB/R, adopted 25 September 1997
US – Shirts and Blouses	Appellate Body Report, <i>United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India</i> , WT/DS33/AB, adopted 23 May 1997
Brazil - Aircraft	Appellate Body Report, <i>Brazil – Export Financing Programme for Aircraft</i> , WT/DS46/AB/R, adopted 20 August 1999
Guatemala – Cement (I)	Appellate Body Report, <i>Guatemala – Anti-Dumping Investigation Regarding Portland Cement from Mexico</i> , WT/DS60/AB/R, adopted 25 November 1998
Canada – Aircraft (21.5)	Panel Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft. Recourse by Brazil to Article 21.5 of the DSU</i> , WT/DS70/RW, adopted 20 August 1999
Canada - Aircraft	Appellate Body Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft</i> , WT/DS70/AB/R, adopted 20 August 1999
US - DRAMS	Panel Report, <i>United States – Anti-Dumping Duty on Dynamic Random Access Memory Semiconductors (DRAMS) of One Megabit or Above from Korea</i> , WT/DS99/R, adopted 19 March 1999
Canada – Dairy	Appellate Body Report, <i>Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products</i> , WT/DS103/AB/R and WT/DS113/AB/R, adopted 27 October 1999.
US - FSC	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporation”</i> , WT/DS108/AB/R, adopted 20 March 2000.
US – FSC (21.5)	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporation” . Recourse to Article 21.5 of the DSU by the European Communities</i> , WT/DS108/AB/RW, adopted 29 January 2002.
Argentina – Footwear	Panel Report, <i>Argentina – Safeguard Measures on Imports of Footwear</i> , WT/DS121/R, adopted 12 January 2000.
Mexico – HFCS (21.5)	Appellate Body Report, <i>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</i> , WT/DS132/AB/RW, adopted 21 November 2001.
Korea - Beef	Panel Report, <i>Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef</i> , WT/DS161/R and WT/DS169/R, adopted 10 January 2001
Chile – Price Band	Appellate Body Report, <i>Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products</i> , WT/DS207/AB/R, adopted 23 October 2002
US – Byrd Amendment	Appellate Body Report, <i>United States – Continued Dumping and Subsidy Offset Act of 2000</i> , WT/DS217/AB/R and WT/DS234/AB/R, adopted 27 January 2003
Canada – Aircraft II	Panel Report, <i>Canada – Export Credits and Loan Guarantees for Regional Aircraft</i> , WT/DS222/R, adopted 19 February 2002.
EC - Sardines	Appellate Body Report, <i>European Communities – Trade Description of Sardines</i> , WT/DS231/AB/R, adopted 23 October 2002.

List of Exhibits

Market Revenue and US Government Payments to US Upland Cotton Producers	<i>Exhibit Bra- 169</i>
PFC, MLA, DP and CCP Payments per Base Acre of Covered Crops	<i>Exhibit Bra- 170</i>
“Counter-Cyclical Payments under the 2002 Farm Bill,” NCC, August 2003	<i>Exhibit Bra- 171</i>
Rice Outlook, USDA, 13 August 2003, Table 1	<i>Exhibit Bra- 172</i>
Revised Estimate of Support Granted by Commodity via Countercyclical Payments.	<i>Exhibit Bra- 173</i>
“Income Protection – Cotton Crop Provisions”, USDA Federal Crop Insurance Corporation, 2000-321	<i>Exhibit Bra- 174</i>
“Cotton Crop Provisions”, USDA Federal Crop Insurance Corporation, 99-021	<i>Exhibit Bra- 175</i>
“Course Grain Crop Provisions”, USDA Federal Crop Insurance Corporation, 98-041	<i>Exhibit Bra- 176</i>
“ERS Briefing Room: Farm Income and Costs: Farm Income Forecasts”	<i>Exhibit Bra- 177</i>
“Facts About Texas and Agriculture”, Texas Cooperative Extension, The Texas A&M University System	<i>Exhibit Bra- 178</i>
JunJie Wu, “Crop Insurance, Acreage Decisions, and Nonpoint-Source Pollution,” American Journal of Agricultural Economics 81, May 1999	<i>Exhibit Bra- 179</i>
Keith J. Collins and Joseph W. Glauber “Will Policy Changes Usher in a New Era of Increased Agricultural Market Variability?”, Second Quarter 1998.	<i>Exhibit Bra- 180</i>
US General Accounting Office, Report to the Ranking Minority Member, Committee on Agriculture, Nutrition and Forestry, US Senate, <i>Former Soviet Union: Creditworthiness of Successor States and US Export Credit Guarantees</i> , GAO/GGD-95-60 (February 1995)	<i>Exhibit Bra- 181</i>
2004 US Budget, Federal Credit Supplement, Table 8	<i>Exhibit Bra- 182</i>
US Budget for FY 1992	<i>Exhibit Bra- 183</i>
US Budget for FY 1993	<i>Exhibit Bra- 184</i>
Congressional Budget Office Staff Memorandum, <i>An Explanation of the Budgetary Changes Under Credit Reform</i> , April 1991	<i>Exhibit Bra- 185</i>
Congressional Research Service Issue Brief for Congress, <i>Agriculture and the Budget</i> , IB95031, (16 February 1996)	<i>Exhibit Bra- 186</i>

O.A. Cleveland Newsletter, 25 April 2003; O.A. Cleveland Newsletter, 8 August 2003 *Exhibit Bra- 187*

Testimony of James Echols, Chairman of the National Cotton Council before the Committee on Agriculture, Nutrition and Forestry of the US Senate, 17 July 2001 *Exhibit Bra- 188*

Cotton and Wool Outlook, USDA, 13 August 2003 *Exhibit Bra- 189*

Affidavit of Marcelo Pinheiro Franco *Exhibit Bra- 190*

I. PRELIMINARY ISSUES

(3) If the request for consultations in this dispute omitted certain products in relation to export credit guarantees, on what basis is it argued that it failed to identify the measures at issue in accordance with Article 4.4 of the DSU?

Brazil's Comment on US Answer:

1. In paragraphs 56 of its 11 August Answer to Question 3, the United States argues that footnote 1 to Brazil's request for consultations does not expand the scope of the request, with regard to the US export credit guarantee programmes, beyond upland cotton. This is inaccurate. The footnote number falls *immediately after the words "upland cotton"* in the first sentence of the first paragraph of the request. With reference to "upland cotton", the footnote reads, "[e]xcept with respect to export credit guarantee programmes as explained below".¹ Although the United States claims that there is no explanation "below", there is indeed such an explanation. In particular, Brazil described its potential claim as follows, on page 4 of the request:

Regarding export credit guarantees, export and market access enhancement provided under the Agricultural Trade Act of 1978, as amended, and other measures such as GSM-102, GSM-103, and SCGP programmes, Brazil is of the view that these programmes, as applied and as such, violate Articles 3.3, 8, 9.1, and 10.1 of the Agreement on Agriculture and are prohibited export subsidies under Article 3.1(a) and item (j) of the Illustrative List of Export Subsidies included in Annex I to the SCM Agreement.²

The Panel will note that there is no limitation in this sentence to any particular commodity or commodities.

2. At paragraph 7 of its 11 August Answer, the United States asserts that "the statement of evidence attached to Brazil's consultation request did not include any evidence related to measures other than those for upland cotton." This too is inaccurate. The United States conveniently leaves the word "available" out of the term "statement of available evidence" used in Articles 4.2 and 7.2 of the SCM Agreement. Brazil was required to provide a statement of the evidence available to it at the time. It was not required to attach exhibits with the evidence; nor was it required to provide a statement regarding all of the evidence that it would eventually present to this Panel. In paragraph 3 of its statement of available evidence, Brazil addressed what it knew at that point about the US export credit guarantee programmes:

US export credit guarantee programmes, since their origin in 1980 and up [to] the present, provide premium rates that are inadequate to cover the long-term operating costs and losses of the programmes; in particular there were losses caused by large-scale defaults totaling billions of dollars that have not been reflected in increased premiums to cover such losses.

3. This sentence speaks not just to the existence of the US export credit guarantee programmes, but also to the way in which they constitute export subsidies, given the explicit use of the language included in item (j) of the Illustrative List of Export Subsidies. The statement fulfils the requirement in Articles 4.2 and 7.2 of the SCM Agreement. The Panel will also note that there is no limitation in this sentence to any particular commodity or commodities.

4. In footnote 3 to its response, the United States states that it "will be making a request for a preliminary ruling" that Brazil's consultation request was broader than its statement of evidence, in

¹ WT/DS/267/1, p. 1.

² WT/DS/267/1, p. 4.

violation of Article 7.2.³ As demonstrated above, Brazil's request, and the accompanying statement of available evidence, do not support the United States' assertion. Both the request and the statement of available evidence address the US export credit guarantee programmes without limitation to any particular commodity or commodities.

5. Moreover, even if the United States were to make this request for a preliminary ruling and the Panel were to grant it, it would not affect Brazil's claims. Brazil's compliance with Article 7.2 of the SCM Agreement can have no effect on its claims under the Agreement on Agriculture, or on its prohibited subsidy claims under the SCM Agreement, or on its actionable subsidy claims with respect to upland cotton.

6. Finally, according to the Panel's Working Procedures, requests for preliminary rulings by a party were to have been made "not later than its first submission to the Panel".⁴ Thus, the US request would not be timely. Brazil submits this information at this stage in the hope of avoiding another lengthy procedural objection by the United States.

(4) Is it argued that the export credit guarantee programmes concerning upland cotton are each a separate or independent measure, in that they operate independently?

Brazil's Comment on US Answer:

7. In paragraph 11 of its 11 August Answer to Question 4, the United States argues that "each export credit guarantee issued is a separate measure". It is not for the United States to define the measures that are the subject of Brazil's challenge. Brazil's requests for consultations and establishment identify the measures at issue as the GSM 102, GSM 103 and SCGP programs, both as such and as applied. In its submissions, Brazil has demonstrated that the programmes constitute export subsidies under Articles 1.1 and 3.1(a) of the SCM Agreement, since they are unique financing vehicles that are not available on the market for agricultural commodity transactions and as such provide something better than is available on the market. Brazil has also demonstrated that the long-term operating costs and losses for the programs outpace premiums collected, under item (j) of the Illustrative List (item (j) speaks to the long-term operating costs and losses of "programmes," and not individual guarantees).

(8) Does the United States confirm that the questions referred to by Brazil in paragraph 92 of Brazil's oral statement were posed to the United States in the consultations?

Brazil's Comment on US Answer:

8. In paragraph 17 of its 11 August Answer, the United States concedes that Brazil posed the questions included at Exhibit Bra-101. The Panel will note that many of the questions included in Section 9 of Brazil's list of questions cover export credit guarantees for all commodities. The United States therefore concedes that Brazil consulted with it on the matters raised in those questions. As Brazil discussed in paragraphs 95-98 of its Statement at the First Meeting of the Panel, panels and the Appellate Body have concluded that for a matter to be properly within the scope of a request for establishment, actual consultations must have been held. That has also been the United States' position in a number of other disputes, including *US – DRAMS* and *Japan – Agricultural Products*.⁵

9. The refusal of the United States to answer Brazil's questions cannot hinder Brazil's ability to pursue its claims against the CCC export guarantee programmes without any limitation to a particular

³ US 11 August Answer to Question 3, para. 7 and footnote 3 to that paragraph.

⁴ Working Procedures of the Panel, 27 May 2003, para. 12.

⁵ Oral Statement of Brazil, para. 96-97.

commodity or commodities. If it did, responding Members would have every incentive to refuse to answer any questions during consultations, thereby halting dispute settlement proceedings altogether.

(10) What actual prejudice, if any, has the United States suffered as a result of the alleged omission of products other than upland cotton from the request for consultations?

Brazil's Comment on US Answer:

10. Brazil agrees that “a Member cannot proceed to a panel unless the Member has consulted on that measure”, as the United States argues in paragraph 19 of its response. Brazil's request for consultations included the CCC export guarantee programmes in connection with all commodities, however, and the United States concedes, in paragraph 17 of its answer to Question 8, that it consulted with Brazil via the list of questions included in Exhibit Bra-101.

11. Brazil does not agree with the United States' assertion, at paragraph 20 of its 11 August Answer, that the consultation request is of a “jurisdictional nature”. While the Appellate Body has concluded that a complaining Member's request for *establishment* is jurisdictional in nature, and strictly delimits a panel's terms of reference⁶, it has not made this statement with respect to a request for *consultations*. In fact, in *Brazil – Aircraft*, the Appellate Body concluded that there is no requirement for a “*precise and exact identity*” between a request for consultations and a request for establishment, which suggests that a request for consultations is *not* jurisdictional in nature.⁷

12. In paragraph 23 of its 11 August Answer, the United States argues, without any proof, that it “has suffered an inability to prepare, respond, and consult with respect to allegations on measures never presented to the United States in accordance with the DSU”. As noted above, Brazil's request for consultations specifically addressed potential claims against the US export credit guarantee programs in connection with all commodities, and not just upland cotton. Moreover, the United States acknowledges that Brazil posed questions to it regarding those programmes in connection with all commodities. The questions were provided to the United States in writing on 22 November, in advance of the consultations session.⁸ In paragraph 92 of its Oral Statement at the First Meeting of the Panel, Brazil offered extracts from those questions, which clarify that consultations regarding the US export credit guarantee programs were not limited to upland cotton.

13. The United States, therefore, was aware, both from Brazil's request for consultations and from Brazil's extensive list of questions, that the consultations included US export credit guarantee programs with respect to all commodities, and not just upland cotton. That the United States refused to respond to Brazil's questions does not mean that it had an “*inability*” to prepare, respond, and consult with Brazil – it means that the United States made a strategic decision not to do so. The United States had more than seven months from receipt of Brazil's questions until it filed its First Submission to “prepare and respond” to Brazil's claims. This demonstrates that no due process rights were violated nor any prejudice caused. The United States alone bears responsibility for any alleged “prejudice” it has suffered as a result of its own strategic decision.

14. In paragraph 24 of its 11 August Answer, the United States argues that it “has not had [sic] proper opportunity to consult” with Brazil on the US export credit guarantee programs with respect to all commodities. In paragraph 17 of its 11 August Answer to Question 8, however, the United States concedes that Brazil did pose questions on the US export credit guarantee programmes with respect to all commodities. Consultations did, therefore, occur with respect to export credit guarantees covering all eligible agricultural products. The United States refused during meetings on 3-4 December, 19 December 2002 and 17 January 2003 to provide answers to Brazil's questions. With its

⁶ Appellate Body Report, *EC – Bananas III*, WT/DS27/AB/R, para. 142.

⁷ Appellate Body Report, *Brazil – Aircraft*, WT/DS46/AB/R, para. 132.

⁸ Exhibit Bra -101 (Brazil's Questions for the Purposes of Consultations, 22 November 2002).

consultations request and its extensive list of questions, however, Brazil fulfilled the requirement to consult with the United States on the full scope of the programmes.

(11) Does the United States agree that Brazil's request for establishment of the Panel can be understood to indicate that Brazil's export credit guarantee claims relates to products other than upland cotton? How, if at all, is this relevant?

Brazil's Comment on US Answer:

15. At paragraphs 96-97 of its Statement at the First Panel Meeting, Brazil noted that in other disputes, the US position has been that "a Member should be permitted to refer a claim to a panel if it was actually raised during consultations, even though it may not have been included in the written request for consultations."⁹ In its 11 August Answer to Question 11, the United States now suggests that its position is different with respect to measures than it is with respect to claims. According to the United States, while a Member can add *claims* not present in its consultations request to its panel request, it cannot add *measures*.¹⁰

16. Brazil repeats that its request for consultations does in fact address the US measures (the GSM 102, GSM 103 and SCGP programs) in connection with all commodities. Every measure included in its request for establishment was similarly included in its request for consultations. The US argument is therefore irrelevant.

17. In any event, the US reliance on the Appellate Body's decision in *Guatemala – Cement (I)* is misplaced.¹¹ In that case, the Appellate Body explained that the text of Article 6 of the DSU and Article 17.4 of the Anti-Dumping Agreement required a distinction between measures and claims. The United States has, however, failed to explain the textual reason why the distinction between measures and claims is relevant *for the purpose of comparing a request for consultations with a request for establishment*. In fact, the Appellate Body has specifically held that Articles 4 and 6 of the DSU do not "require a *precise and exact identity* between the specific measures that were the subject of consultations and the specific measures identified in the request for the establishment of a panel".¹² Nor has the United States offered any logical reason why a Member should be allowed to add claims not covered by its consultations request to its request for establishment, but not measures. If anything, a defending Member would seem to suffer greater prejudice by the addition of claims than by the addition of measures, since the Member is likely more familiar with its *own* measures than it would be with *another Member's* claims.

(16) What, if any, prejudice in terms of presentation of its case does the United States allege, should the Panel proceed to consider the measures constituting the cottonseed payments under the Agriculture Assistance Act of 2003?

Brazil's Comment on US Answer:

18. There have been many disputes in which Panel found that measures, which were replacement measures to measures originally consulted on, were included in the panel's terms of reference, *Korea – Beef*³ and *Chile- Agricultural Products (Price Band)*¹⁴, to name a few. The Agricultural Assistance Act of 2003 is in the nature of a revised measure, as Brazil has argued in paragraphs 145-150 of its

⁹ Panel Report, *US – DRAMS*, WT/DS99/R, para. 6.8.

¹⁰ US 11 August Answer to Question 11, para. 25.

¹¹ US 11 August Answer to Question 11, para. 26 note 9

¹² Appellate Body Report, *Brazil – Aircraft*, WT/DS46/AB/R, para. 132.

¹³ Panel Report, *Korea – Beef*, WT/DS161/R and WT/DS169/R, para. 563-564.

¹⁴ Appellate Body Report, *Chile – Agricultural Products (Price Band)*, WT/DS207/AB/R, para. 143-

Oral Statement. Brazil also notes that the United States has identified no prejudice to its ability to defend this measure in this dispute.

- (17) (a) **What is the relationship of the Agricultural Assistance Act of 2003 to other legislation in the request for establishment of the Panel?**
- (b) **Do the legal instruments follow directly one after another, or are there temporal gaps? Are payments authorized under a broad legislative authority or are they specific to each legal instrument?**
- (c) **Please provide any implementing regulations. Do these implementing regulations resemble those relating to previous programmes or payments? Are payments made retrospectively? How if at all is this relevant?**

Brazil's Comment on US Answer

19. The United States argues that the four legislative acts that authorize cottonseed payments for the MY 1999, 2000 and 2002 crop are completely unrelated measures and that – while the regulations implementing these payments are very similar – this is immaterial to the question of whether such payments are part of a single programme.¹⁵

20. If a Member like Brazil would be prevented from challenging yearly renewed measures that provide support under the very same mechanism – and in fact under nearly identical regulations¹⁶ – than another Member like the United States could continue to enact yearly measures and limit the challenge by WTO Members to old measures without a prevailing challenge having any effect on its current and future identical measures. The result would put a complaining Member in the impossible situation of having to challenge identical measures year after year, just because they are based on legislation that “bears no relation”¹⁷ to preceding *identical* legislation *on the same matter*.

21. The Panel in *Argentina – Footwear* rejected similar arguments to those made by the United States:

Moreover, it appears that an interpretation whereby these subsequent Resolutions are considered to be measures separate and independent from the definitive safeguard measure, and thus outside our terms of reference, could be contrary to Article 3.3 of the DSU. Such an interpretation could allow a situation where a matter brought to the DSB for prompt settlement is not *resolved when the defendant changes the legal form of the measure through a separate but closely related instrument, while the measure in dispute remains essentially the same in substance*. In this way, Members could always keep one step ahead of any WTO dispute settlement proceeding because in such a situation, the complaining Member would indeed, challenge a “moving target”, and panel and Appellate Body’s findings could already be overtaken by events when they are rendered and adopted by the DSB.¹⁸

22. Brazil maintains that the Agricultural Assistance Act of 2003 constitutes a subsequent, separate but closely related instrument, that is essentially the same as the legal instruments authorizing the MY 1999 and MY 2000 cottonseed payments and that is, therefore, within the Panel’s terms of reference.

¹⁵ US 11 August Answer to Question 17, para. 39-43.

¹⁶ Compare Exhibit US14-US16.

¹⁷ US 11 August Answer to Question 17, para. 39.

¹⁸ Panel Report, *Argentina – Footwear*, WT/DS121/R, para. 8.41 (emphasis added).

II. ARTICLE 13(B): DOMESTIC SUPPORT MEASURES

A. "EXEMPT FROM ACTIONS"

(20) In paragraph 8 of its initial brief (dated 5 June, 2003), the United States argued that the word "actions" as used in the phrase "exempt from actions" in Article 13 of the Agreement on Agriculture includes the "bringing of a case" and consultations. In paragraph 36 of its first written submission (dated 11 July, 2003), the United States stated as follows:

"[P]rior to this point in the process, the DSU rules did not afford the United States any opportunity to prevent the dispute from proceeding through consultations and panel establishment automatically, regardless of the US insistence that its measures conform to the Peace Clause."

Is it the United States' understanding that the drafters used the phrase "exempt from actions" knowing that under the DSU it would not be possible fully to exempt "actions", as the United States interprets that term?

(21) In *US - FSC* and *US - FSC (21.5)* the Appellate Body made findings under the SCM Agreement relating to export subsidies in respect of agricultural products without making a finding in respect of Article 13 of the Agreement on Agriculture. How is this relevant to the United States' interpretation of the phrase "exempt from actions" as used in Article 13? USA

Brazil's Comment on US Answers:

23. The United States and the European Communities maintain that the complaining party has the burden of proof under Article 13 of the Agreement on Agriculture. More specifically, they claim that Article 13 is not in the nature of an affirmative defence. Brazil's comment will again show that their position is untenable.

24. In its 11 August Answer to Question 20 of the Panel, the United States asserts, under the "exempt from action" argument, that "Brazil has attempted to improperly invoke dispute settlement procedures notwithstanding the Peace Clause."¹⁹ According to the United States, a dispute settlement procedure could only be initiated after a determination of non-compliance with Article 13 has been made. In its 11 August Answer to Question 21, the United States then dismisses the findings in *US - FSC* by simply stating that they do not address the peace clause and that the issue was not raised by either party in that case.²⁰ Therefore, those rulings and recommendations "provide no guidance for purposes of this dispute".

25. The EC maintains that "Article 13 is more akin to a threshold permitting further action if the threshold is not complied with."²¹ The EC affirms that Article 13 "is an integral part of the *Agreement on Agriculture*".²² In that sense it would be comparable to Article 6 of the ATC, Article 3.3 of the SPS Agreement, and Article 2.4 of the TBT Agreement, which were found not to be affirmative defences by the Appellate Body.²³ According to the EC, those provisions, like Article 13 of the Agreement on Agriculture, "provide certain rights to WTO Members, but cannot be seen as exceptions".²⁴

¹⁹ US 11 August Answer to Question 20, para. 47.

²⁰ US 11 August Answer to Question 21, para. 48.

²¹ Third Party Submission of the EC, para. 11.

²² Third Party Submission of the EC, para. 12.

²³ Third Party Submission of the EC, para. 12.

²⁴ Third Party Submission of the EC, para. 12.

26. Brazil disagrees. The Appellate Body addressed the issue of burden of proof on numerous occasions. In *US – Shirts and Blouses*, the Appellate Body made a general finding stating that

... the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence. If that party adduces evidence sufficient to raise a presumption that what is claimed is true, the burden then shifts to the other party, who will fail unless it adduces sufficient evidence to rebut the presumption.

In the context of the GATT 1994 and the WTO Agreement, precisely how much and precisely what kind of evidence will be required to establish such a presumption will necessarily vary from measure to measure, provision to provision, and case to case.²⁵

27. When examining Article 6 of the ATC, Article 3.3 of the SPS Agreement, and Article 2.4 of the TBT Agreement, the Appellate Body did not stray from this principle. In fact, it was the cornerstone of all determinations concerning the above-cited provisions. Paragraph 275 of the Appellate Body report in *EC – Sardines* reads:

In *EC – Hormones*, we found that a "general rule-exception" relationship between Articles 3.1 and 3.3 of the SPS Agreement does not exist, with the consequence that *the complainant had to establish a case of inconsistency with both Articles 3.1 and 3.3*.¹⁹⁶ We reached this conclusion as a consequence of our finding there that "Article 3.1 of the SPS Agreement simply excludes from its scope of application the kinds of situations covered by Article 3.3 of that Agreement".¹⁹⁷ Similarly, the circumstances envisaged in the second part of Article 2.4 are excluded from the scope of application of the first part of Article 2.4. Accordingly, as with Articles 3.1 and 3.3 of the SPS Agreement, there is no "general rule-exception" relationship between the first and the second parts of Article 2.4. Hence, in this case, it is for Peru – *as the complaining Member seeking a ruling on the inconsistency with Article 2.4 of the TBT Agreement* of the measure applied by the European Communities – to bear the burden of proving its claim. (emphasis added) (footnotes omitted)²⁶

28. With regard to Article 6 of the ATC, the Appellate Body found that provision to be a fundamental part of the rights and obligations of WTO Members concerning non-integrated textile and clothing products covered by the ATC during the transition period. Consequently a party claiming a violation of a provision of the WTO Agreement by another Member must assert and prove its claim. In this case, *India claimed a violation by the United States of Article 6 of the ATC*. We agree with the Panel that it, therefore, was up to India to put forward evidence and legal argument sufficient to demonstrate that the transitional safeguard action by the United States was inconsistent with the obligations assumed by the United States under Articles 2 and 6 of the ATC. (emphasis added)²⁷

29. Unlike the EC, Brazil believes that these Appellate Body findings underscore the striking differences between Article 13 of the Agreement on Agriculture and the other provisions cited by the EC and which the Appellate Body found not to be in the nature of an affirmative defence.

30. First, Brazil notes that in all Appellate Body findings, the complaining party claimed a violation of the provision at issue. The complaining party tried to impute the burden of proof on the respondent by alleging that those provisions also contained language that provided an opportunity for an affirmative defence under an "exception" to the general rule.

²⁵ Appellate Body Report, *US – Shirts and Blouses*, p. 14.

²⁶ Appellate Body Report, *EC – Sardines*, para. 275.

²⁷ Appellate Body Report, *US – Shirts and Blouses*, p. 16.

31. Article 13 of the Agreement on Agriculture is entirely different. The peace clause imposes no obligations on WTO Members. As the EC rightfully stated in paragraph 6 of its Initial Submission of 10 June 2003:

a Member is not under an obligation to act consistently with Article 13 of the *Agreement on Agriculture* – failing to respect Article 13 implies that a Member no longer enjoys protection thereof. Consequently ... Article 13 of the *Agreement on Agriculture* can only be seen as a defence against a claim brought under other aspects of the WTO Agreements which regulate the provision of subsidies. It would seem bizarre if before Brazil could bring a claim with respect to subsidies which it considered did not respect the US's obligations, Brazil had first to establish that potential defences did not apply. (italics in original) (underlining added)²⁸

32. Brazil entirely agrees with the characterization of Article 13 as a potential defence against claims brought before the WTO. In fact, as the Panel is well aware, in Brazil's request for the establishment of the Panel, Brazil does not claim that the United States violated Article 13. Such violation is indeed impossible, since Article 13 of the Agreement on Agriculture imposes no obligations whatsoever on WTO Members. Article 13 simply provides shelter to Members that invoke its exemption from actions based on certain other provisions of the WTO Agreements. Again, as the Appellate Body stressed every single time it addressed the issue, "the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence."²⁹

33. Second, Brazil's interpretation is entirely compatible with the findings of the panel and the Appellate Body in *US – FSC*. Brazil, unlike the United States, considers these finding to be very relevant to this dispute. In *US – FSC*, the United States decided not to invoke Article 13 of the Agreement on Agriculture as a possible defence against the challenges brought by the EC. The panel and the Appellate Body did not need to address Article 13 simply because it was not used as a defence by the respondent. This situation is not necessarily unusual. For example, a respondent that knows, in advance, that it is not complying with the requirements of Article 13, may well choose to directly rebut the prima facie case of the complainant by providing rebuttal arguments and evidence without attempting to use the Article 13 shelter.

34. Indeed, interpreting Article 13 of the Agreement on Agriculture as a "threshold"³⁰ provision is at odds with the Appellate Body's findings in *US – FSC*, *US – FSC (21.5)*, *Mexico – HFCS (21.5)* and *US – Byrd Amendment*. In *Mexico – HFCS (21.5)*, the Appellate Body held that

We believe that a panel comes under a duty to address issues in at least two instances. First, as a matter of due process, and the proper exercise of the judicial function, panels are required to address issues that are put before them by the parties to a dispute. Second, *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 the lawful panel proceeding.' 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*. (emphasis added) (footnote omitted)³¹

²⁸ Initial Third Party Submission of the EC, para. 6.

²⁹ Appellate Body Report, *US – Shirts and Blouses*, p. 14.

³⁰ Third Party Submission of the EC, para. 11.

³¹ Appellate Body Report, *Mexico – HFCS (21.5)*, WT/DS132/AB/RW, para. 36.

35. The Appellate Body applied this reasoning to itself in *US – Byrd Amendment*. In that case, the Appellate Body examined an issue related to the Panels jurisdiction, although it was not addressed before the Panel or, indeed mentioned in the notice of appeal.³² If Article 13 of the Agreement on Agriculture were a threshold provision affecting the jurisdiction of a panel or the Appellate Body, both the panels and the Appellate Body in *US – FSC* and *US – FSC (21.5)* would have had to address the issue of peace clause exemption of the claims brought by the EC. The fact that none of them did is further evidence that Article 13 is not a “threshold” or jurisdictional provision. As Brazil maintains, Article 13 of the Agreement on Agriculture is an affirmative defence.

36. Further, Brazil does not claim that Article 13 is an “exception”. Brazil does not claim that the United States “violated” Article 13 and, therefore, Brazil does not bear the burden of proving any such assertion. Actually, Brazil simply does not believe that Article 13 is at all relevant to claims raised under the SCM Agreement or GATT Article XVI until the respondent claims that it is exempt by the provisions of the peace clause. The respondent claiming such exemption has the burden of proving that it is entitled to it.³³ If the respondent does not claim such protection, Article 13 is moot, as demonstrated by the *US – FSC* case.

37. In paragraph 11 of its Oral Statement of 24 July, the EC points out that no “credible response” was given to the argument it put forward suggesting that Brazil’s approach “has perverse effects”.³⁴ The EC claimed that

if Article 13 is considered an affirmative defence, when a complainant brings a dispute under Articles 5 and 6 of the SCM Agreement and, for instance, Article 6 of the *Agreement on Agriculture*, the complainant would be required to prove a breach of Article 6 while at the same time the defendant would also be required to prove that it had not infringed Article 6 of the Agreement. The burden of proof cannot switch between parties simply on the basis of whether the complainant cites the *SCM Agreement* or not ...” (italics on the original)³⁵

38. Brazil fails to see the conundrum that seems to puzzle the EC. If the complainant cites the SCM Agreement or, better still, alleges a violation of the SCM Agreement together with a violation of Article 6 of the *Agreement on Agriculture*, the burden of proving both assertions rests on the complainant irrespective of the fact that the respondent may invoke Article 13. If the complainant fails to establish the violation of Article 6 of the *Agreement on Agriculture*, then the task of the respondent to invoke the Article 13 shelter against a possible violation of the SCM Agreement is made that much easier. In fact, the burden of proof concerning the violation of Article 6 of the *Agreement on Agriculture* will simply start with the complainant. As the Appellate Body noted in *US – Shirts and Blouses*, if the complainant “adduces evidence sufficient to raise a presumption that what is claimed is true, the burden shifts to the other party, who will fail unless it adduces sufficient evidence to rebut the presumption”. Therefore, the burden of proof may well switch between parties, but not “on the basis of whether the complainant cites the *SCM Agreement*”, as the EC suggested in its Oral Statement.

39. In sum, Brazil reemphasizes that the peace clause is in the nature of an affirmative defence.

³² Appellate Body Report, *US – Byrd Amendment*, WT/DS217/AB/R and WT/DS234/AB/R, para. 206-208.

³³ Appellate Body Report, *US – Shirts and Blouses*, p. 14.

³⁴ Oral Statement of the EC, para. 11

³⁵ Oral Statement of the EC, para. 11.

B. "SUCH MEASURES" AND ANNEX 2 OF THE AGREEMENT ON AGRICULTURE

(22) Please explain the difference, if any, between the meaning of "defined" and the meaning of "fixed" in the phrase "a defined and fixed base period" in paragraph 6(a) of Annex 2 of the Agreement on Agriculture.

Brazil's Comment on US Answer:

40. The United States 11 August Answer to Question 22 renders the meaning of the word "fixed" meaningless by isolating the phrase "relative position" from the full dictionary definition.³⁶ The complete definition includes the phrase "definite, permanent, and lasting".³⁷ There is nothing "permanent" about the US interpretation of the meaning of "fixed base period" for the PFC and direct payment programmes. For further comments on the issue, Brazil refers the Panel to paragraphs 10-12 of its Rebuttal Submission.

(24) How often can a Member define and fix a base period in accordance with paragraph 6 of Annex 2 of the Agreement on Agriculture?

Brazil's Comment on US Answer:

41. Brazil agrees with the United States' statement that there is "no requirement in paragraph 6 that a particular base period be used for a decoupled income support measure nor that the same base period be used for purposes of every decoupled income support measure."³⁸ But this misses the point. The legal and factual question is whether a measure for which a new base period is "*fixed*" has the same structure, design, and eligibility criteria as an older replaced measure which had a *different* base period. The evidence demonstrates that PFC payments and direct payments have a similar structure, design, and eligibility criteria.³⁹

(29) Please explain the meaning of the words "the fundamental requirement" as used in paragraph 1 of Annex 2 of the Agreement on Agriculture.

Brazil's Comment on US Answer:

42. The United States argues in response to this question that "compliance with the fundamental requirement of the first sentence will be demonstrated by conforming to the basic criteria of the second sentence plus the applicable policy-specific criteria of paragraphs 6-13."⁴⁰ Brazil disagrees that compliance with the basic and policy-specific criteria is a sufficient condition for compliance with the fundamental requirement. For example, the volume of direct payments that conform to the criteria in paragraph 6 is not limited. However, the amount of support a Member provides may be so large that the payments create significant production and trade-distorting effects. Therefore, even if direct payments conform to the basic and policy-specific criteria in Annex 2, they may still have considerable production and trade-distorting effects. Brazil refers to its arguments in support of the "stand-alone" nature of the fundamental requirement.⁴¹

³⁶ Brazil 11 August Answer to Question 22, para. 20.

³⁷ The New Shorter Oxford English Dictionary, 1993 edition, p. 962.

³⁸ US 11 August Answer to Question 24.

³⁹ See Rebuttal Submission of Brazil, para. 10.

⁴⁰ US 11 August Answer to Question 29, para. 59.

⁴¹ First Submission of Brazil, para. 163-165; Brazil's 11 August Answer to Questions 27-28, para. 32-

(32) If the first sentence of paragraph 1 of Annex 2 expresses a general principle which informs the interpretation of the criteria in Annex 2, please explain how this affects the assessment of the direct payments programme's compliance with paragraph 6 of Annex 2.

Brazil's Comment on US Answer:

43. Contrary to the US argument at paragraph 68 of its 11 August Answers, there is no conflict between the Brazil's position regarding the fruits, vegetables and wild rice prohibition and Annex 2, paragraph 1 'fundamental requirement'. The undisputed facts show that this prohibition on the production of certain crops channels production to other crops that are permitted to be produced to receive the payment.⁴² This channeling of payments creates production and trade distorting effects inconsistent with Annex 2, paragraph 1.

44. Further, the United States engages in a wishful interpretation when it states in paragraph 68 of its 11 August Answer that "paragraph 6(b) should be read to prevent a Member from requiring a recipient to produce certain crops". This interpretation would render Annex 2, paragraph 6(e) a nullity. Paragraph 6(e) provides that "no production shall be required in order to receive such payments". The US interpretation of paragraph 6(b) as not requiring the production of "certain crops" is the same as 6(e)'s prohibition on not requiring production of "any crops".

45. Paragraph 6(b) is distinct from paragraph 6(e) because it provides a clear test that *the amount* of payment cannot be related to the type of production. There is no factual dispute among the parties that the amount of PFC and direct payments *falls* when base acres are used to produce fruits, vegetables, tree nuts, and wild rice. There is no factual dispute that the 1996 FAIR Act and the 2002 FSRI Act *require* the prohibition or reduction in payments if these crops are produced on base acreage. Given these two undisputed facts and the clear text of Annex 2, paragraph 6(b), the only conclusion is that PFC and direct payments do not meet the policy specific criteria of Annex 2.

C. "DO NOT GRANT SUPPORT TO A SPECIFIC COMMODITY"

(33) According to the United States' interpretation of the word "grant", when can a Member claim that a measure is not exempt from action under Article 13(b)? what if the measures is enacted annually? Can the Member obtain a remedy in respect of that measure under the DSU?

Brazil Comment to US Answer:

46. Brazil's addresses in detail the US "statute of limitations" argument at paragraphs 88-96 of its Rebuttal Submission, as well as at paragraphs 40-47 of its Oral Statement.

(37) In the United States' view, why did the drafters not use the exact term "product-specific" in Article 13(b)(ii)?

Brazil Comment on US Answer:

47. The United States' 11 August Answer once again reveals that it equates the term "support to a specific commodity" with "product-specific". Brazil notes again that neither the phrase "product-specific" nor "AMS" is found in the text of Article 13(b). Given the use of such terms in the Agreement on Agriculture, the Drafters must be presumed to have used the term "support to a specific commodity" for a reason. The US answer ignores the likely reason which is that "support to a specific commodity" is qualified by the term "such measures" which includes the universe of non-

⁴² See Rebuttal Submission of Brazil, para. 7.

green box support measures in the *chapeau* to Article 13(b). This universe of measures from which such support may be found is not limited to simply “product-specific” measures.

(38) Given the fact that subsidies available for more than one product could have various effects on production, how does the United States demarcate between product-specific support and non-product specific support?

Brazil’s Comment on US Answer:

48. The United States demarcation line does not take into account the definition of “non-product specific” in Article 1(a) which is “provided in favour of agricultural producers *in general*”. This “in general” language shows where the line between product-specific and non-product specific must be drawn. Any support that is *not* provided to producers “*in general*” cannot, by definition, be non-product specific support. It must instead fall into the category of “product-specific support”. The United States fails to recognize that the term “in general” is directly related to and qualifies the phrase “support . . . provided for an agricultural product in favour of the producers of the basic agricultural product”.

49. The “demarcation” line drawn by the United States between “product-specific” and “non-product specific” support is necessary to justify the narrow US specificity test for Article 13(b)(ii). The United States argues that support could only be “product-specific” if “production is necessary for the support to be received.”⁴³ Yet, the Article 1(a) notion of “support” “provided for an agricultural product in favour of the producers of the basic agricultural product” is very broad. It could include any *type* of support, regardless of whether production was required or not. For example, if the facts demonstrate that \$1 billion of support were received by the “producers of a basic agricultural product” (such as in the case of CCP payments to upland cotton producers in MY 2002), the language of Article 1(a) would support the finding that this support is “product-specific”. The only restraint on such a conclusion is if it could be shown that all, or most of the producers of agricultural products received the same type of support. However, none of the five domestic support payments at issue in this dispute comes even close to such an “in general” finding. The inclusion of such subsidies as “support to a specific commodity” is confirmed by the context of Article 13(b)(ii) which includes Annex 3 of the Agreement on Agriculture as discussed in paragraphs 17-22 of Brazil’s Rebuttal Submission.

50. Further, the United States never addresses the premise of the Panel’s question, i.e., that subsidies for more than one product could have various effects on production. This is exactly the situation with PFC, market loss, direct payments, CCP payments, and crop insurance subsidies. The evidence (which consists in large part of the statements of present or former USDA economists) shows the production enhancing effects of each of these subsidies.

51. The US 11 August Answer highlights the narrowness of its Article 13(b)(ii) specificity test. Trade and production-distorting amber box support from each of these five subsidies increases US production and sustains high levels of US exports of upland cotton. Yet, under the US specificity test, it could never be deemed “support to” upland cotton because no production of upland cotton is legally required. The Panel should reject this approach and find that these programmes provide support to upland cotton.

(39) If “such measures” in Article 13(b)(ii) refers to all those in the chapeau of Article 13(b), why are they not included in the potential comparisons with 1992? In what circumstances can measures which grant non-product specific support lose exemption from action under Articles 5 and 6 of the SCM Agreement and Article XVI of GATT 1994?

⁴³ US 11 August Answer to Question 38, para. 81.

Brazil Comment to US Answer:

52. The United States 11 August Answer does not address the second of the Panel's questions directly. But based on the argument in the "answer," the direct answer to the question would have been "*there are no circumstances in which measures which grant non-product specific support lose exemption from action under Articles 5 and 6 of the SCM Agreement and Article XVI of GATT 1994.*" The arguments presented by the United States in its answer confirms that its interpretation creates a broad new category of "exempt" non-green box support – those presumptively trade and production-distorting measures it labels "non-product specific". The US constructs this new exempt category by improperly interpreting the phrase "product-specific" to include only non-green box support legally requiring the production of upland cotton. This incorrect definition is inconsistent with the fact that in analogous situations involving calculation of AMS, paragraphs 12-13 of Annex 3 of the Agreement on Agriculture require all types of non-green box support providing support to the producers of an agricultural commodity be included in the amount tabulated. These points are further discussed in paragraphs 13-67 of Brazil's Rebuttal Submission.

53. The US 11 August Answer to the first question in paragraph 84 indicates that it interprets the phrase "such measures" as only including "product-specific" support. Even apart from the incorrect US definition, such an interpretation renders a nullity the reference to most of the "measures" referred to in the "such measures" phrase of Article 13(b)(ii). If the drafters had intended to limit the universe of non-green box support in the manner suggested by the United States, they would have used the phrase "product-specific" instead of "such measures". The better interpretation that does not render the *chapeau* a nullity is that suggested by Brazil: any type of support listed in the *chapeau* which provides "support to a specific commodity" must be included within the support to be counted for the purpose of the required 13(b)(ii) comparison.

D. "IN EXCESS OF THAT DECIDED DURING THE 1992 MARKETING YEAR"

General Comment by Brazil on the US Answers to Questions 47-69

54. Brazil notes that the United States has not fully answered many of the questions posed by the Panel. The United States further announced in various questions that it would provide its views on certain questions posed by the Panel in its rebuttal submission. In the answers provided, the United States has continued to pursue its overly simplistic view of an alleged "decision" to provide a rate of support of 72.9 cents per pound in MY 1992. Brazil has pointed out that this rate of support does not accurately reflect the operation of the US support system to upland cotton and that it ignores restrictions on the availability of support and costs associated with the participation in the support programmes.⁴⁴ Professor Sumner has attempted to correct the overly simplistic US approach and has presented data to that respect.⁴⁵

55. A fundamental flaw exposed by the US 11 August Answers is the inability of the US "72.9 methodology" to account for a number of different types of "support to upland cotton". In its 11 August Answer to Question 67, the United States provides a calculation of upland cotton AMS that lists as "product-specific" support Step 2 payments (user marketing certificates), cottonseed payments, storage payments, and interest subsidies, in addition to deficiency payments, and marketing loan payments. Yet, the United States "72.9 methodology" does not – and cannot – account for cottonseed payments, Step 2 payments, storage payments and interest rate subsidies. The United States takes no account of these subsidies – no matter how large the expenditures may be – because they do not fit within the US methodology. So they simply disappear.

⁴⁴ Oral Statement of Brazil, para. 36; Brazil's 11 August Answer to Question 66(c), para. 120-128.

⁴⁵ See Exhibit Bra-105 (Statement of Professor Sumner at the First Meeting of the Panel).

56. Any methodology that cannot account for *all* of the support “decided” and “granted” in MY 1992 and during the implementation period cannot be legitimate. A methodology that would sanction the cover-up of hundreds of millions – if not billions – of dollars of expenditures cannot be justified by the object and purpose of Agreement on Agriculture or by any reasonable reading of the text of Article 13(b)(ii).

57. With these general points in mind, Brazil comments on the answers provided by the United States.

(43) What are the precise differences between deficiency payments and counter-cyclical payments that lead you to classify the former as product-specific and the latter as non-product specific? How do you classify market loss assistance payments?

Brazil’s Comment on US Answer:

58. The US 11 August Answer at paragraph 87-90 reveals its erroneous interpretation of the phrase “product-specific” in Article 1(a) of the Agreement on Agriculture. The United States ignores the phrase “in general” and assumes that “non-product specific” support is a huge residual category of support that includes everything *except* support which *requires* production of a specific product. Further, the United States’ answer ignores the fact that all types of support in favour of domestic producers of a basic commodity are included in the analogous AMS calculation of Annex 3 – including “product-specific” support where the recipient is *not* required to produce a specific commodity. Brazil outlines the erroneous US interpretation in paragraphs 13-23 of its Rebuttal Submission.

59. The improper narrow US interpretation of “product-specific” is highlighted in its discussion of counter-cyclical payments where the only relevant fact is that a producer receiving CCP payments need not plant any crop at all. Brazil addresses in detail the evidence demonstrating that CCP payments are “support to” upland cotton in paragraphs 48-52 of its Rebuttal Submission.

60. With respect to market loss assistance payments, Brazil notes that it provides a detailed analysis of how such payments are “support to upland cotton” in paragraphs 29-35 of its Rebuttal Submission, as well as in paragraphs 50-54 of its Oral Statement. Contrary to the US statement in paragraph 92 of its 11 August Answers, Brazil has always asserted that market loss assistance payments are “support to a specific commodity”, i.e., to upland cotton.

(46) What is the relevance, if any, of the concept of “specificity” in Article 2 of the SCM Agreement and reference to “a product” or “subsidized product” in certain provisions of the SCM Agreement to the meaning of “support to a specific commodity” in Article 13(b)(ii) Agreement on Agriculture?

Brazil’s comment to US Answer:

61. For the reasons set forth in Brazil’s 11 August Answer to this question, Brazil believes that Article 2 of the SCM Agreement provides useful context in interpreting the concept of specificity in Article 13(b)(ii). Brazil notes that the very narrow US notion of specificity (only support *requiring* recipients to produce the commodity in question) for Article 13(b)(ii) is quite different than the very broad concept of specificity applying to all commodities (including agricultural commodities) as set out in the US SAA referred to in Brazil’s answer. The United States has not provided any reasons why there should be such a radically different concept of specificity involving non-green box domestic support measures under Article 13(b)(ii) and all types of products (including agricultural goods) under the SCM Agreement. Brazil sees no basis for such a significant difference.

(48) Does Article 13(b)(ii) require a comparison of support granted with support decided? How could such a comparison be made?

Brazil's Comment on US Answer:

62. Brazil comments on the US 11 August Answer to Question 48 in the context of its Rebuttal Submission at paragraphs 68-96.

(54) Please identify all United States legal and regulatory and administrative instruments decided during the marketing year 1992, with the respective dates of decision, that decided support for upland cotton.

Brazil's Comment on US Answer:

63. As Brazil has noted in its general comment at paragraphs 54-57 above, the United States focuses solely on the alleged target price decision of 72.9 cents per pound. This simplistic approach does not accurately reflect the actual operation of the US support programmes to upland cotton. As detailed by Professor Sumner in his Statement at the First Meeting, the United States took a number of decisions concerning support for the 1992 marketing year.⁴⁶

64. Professor Sumner – who actually participated in the decision making process concerning the MY 1992 acreage reduction programme decision – explained during the First Meeting of the Panel that the decision on the percentage of upland cotton base that farmers participating in the deficiency payment programme had to leave idle was a conscious decision based on, *inter alia*, budgetary considerations. Given expectations about production and prices in the upcoming marketing year, the decision on the acreage reduction programme was also a decision on expected participation. The United States could base expected participation on historical experience about participation in the deficiency payment program. Professor Sumner indicated that USDA was able to fairly accurately predict actual participation. The decision on the amount of mandatory acreage reduction is, thus, a decision on the level of participation.

65. Professor Sumner's testimony is supported by the Chief and Deputy Chief Economist of USDA who have explained that the aim of the acreage reduction programme was "to balance supply and demand"⁴⁷, i.e., to influence prices and thereby US budgetary outlays. They furthermore report that the United States implemented the acreage reduction programme with a view of reducing costly government stocks, and that the United States – with further budget considerations in mind – reduced target prices.⁴⁸

66. Furthermore, the United States ignores various required additional administrative decisions that were necessary to make its domestic support programmes operative. These decisions include decisions on the deficiency payment rate, on weekly Step 2 payment rates and on a weekly-determined adjusted world price setting the amounts of marketing loan benefits available for that week. By taking all of these decisions, the United States directly influenced the expenditures related to the MY 1992 crop.⁴⁹ In addition, as the United States now reflects in its AMS data, the

⁴⁶ Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting, para. 7-8).

⁴⁷ Exhibit Bra-180 ("Will Policy Changes Usher in a New Era of Increased Agricultural Market Variability?," Keith J. Collins, Joseph W. Glauber, Choices, Second Quarter 1998, p. 27).

⁴⁸ Exhibit Bra-180 ("Will Policy Changes Usher in a New Era of Increased Agricultural Market Variability?," Keith J. Collins, Joseph W. Glauber, Choices, Second Quarter 1998, p. 27).

⁴⁹ Brazil acknowledges that the United States could not possibly determine its expenditures as they would depend to a certain extent on market prices that were also influenced by factors outside the control of the US Government.

United States considers storage payments and interest subsidies⁵⁰ as product-specific support to upland cotton. Consequently, under the US approach, these product-specific domestic support measures need to be taken into account for purposes of the Article 13(b)(ii) decision. Yet, the United States fails to account for these programmes in its list of decisions taken concerning support to upland cotton, just as it failed to account for various decisions relating to the deficiency payment, marketing loan and Step 2 programmes.

67. Brazil also notes that the United States failed to answer Question 54 that asked the United States to identify “all” instruments that decided support for upland cotton. This would also cover instruments other than product-specific instruments. However, the United States has only followed its simplistic view of what kind of decision it took and has not provided information on other decisions. This appears to be an attempt to avoid the conclusion under all other approaches: that the United States provided support in MY 1999-2002 in excess of that decided during the 1992 marketing year.

(55) Please provide a copy of the instruments in which the rate of support for upland cotton during the marketing year 1992 was decided, indicating the date of the decision.

Brazil’s Comment on US Answer:

68. As noted in Brazil’s Comment to the previous question, the United States failed to identify a list of decisions taken with respect to support for upland cotton in MY 1992. As a consequence, the United States also failed to provide copies of those instruments.⁵¹

(57) If the United States decided on a rate of support for MY1992, does that not mean that it decided on whatever budgetary outlay was required to meet that rate of support, even if the exact amount was not known at that time?

Brazil’s Comment on US Answer:

69. At the outset, Brazil refers the Panel to the general comment made in respect of the set of questions referring to the term “decision” in Article 13(b)(ii) of the Agreement on Agriculture. Also this answer suffers from the simplistic picture the United States draws of its MY 1992 support programmes to upland cotton.

70. Brazil disagrees with the United States that it could not be said that the United States decided on budgetary outlays. Indeed, for *all* of the US programmes, there was a decision to authorize whatever budgetary outlays would be necessary to meet the rate of support.⁵² In addition, the United States ignores that it has admitted that there were other programmes that meet its definition of “product-specific” and that do not provide a rate of support: Step 2, cottonseed, storage payments and interest subsidies. The United States accounted for those subsidies by providing budgetary outlays in its upland cotton AMS calculation, but it does not provide any information on the decision taken with respect to those domestic support measures and the rate of support provided by them. In addition, the United States took specific administrative decisions on the deficiency payment rate for MY 1992 (20.3 cents per pound⁵³), weekly Step 2 payment rates as well as weekly decision on the adjusted world price and, thus, the rate of marketing loan benefits. By taking these decisions, the United States decided on the payment rates that resulted from the “rate of support” and, therefore, on the amount of budgetary outlays it would use from its unlimited spending authority.

⁵⁰ Brazil notes that the United States nowhere provides any information concerning the type and conditions of payments that are covered by these terms.

⁵¹ See paras. 63-67 *supra*.

⁵² First Submission of Brazil, para. 141.

⁵³ Exhibit Bra-4 (“Fact Sheet: Upland Cotton,” USDA, January 2003, p. 5).

71. Brazil further disagrees with the US assertion at paragraph 113 of its 11 August Answers that the programs decided by the United States required an unlimited budgetary authority in both MY 1992 and in later marketing years.⁵⁴ Even at prices of zero cents per pound, the amount of US expenditure for the deficiency payment and the marketing loan programme in MY 1992 was, in fact, limited by decisions restricting the participation in the programs to farmers that historically had grown upland cotton, who were eligible, and who decided to participate based on the eligibility criteria. By contrast, participation in the MY 2002 marketing loan programme, the crop insurance programme, and the Step 2 programme, for instance, is no longer limited and now has an unlimited budgetary authority coupled with mandatory payment provisions. In particular, the marketing loan programme is now unlimited whereas in MY 1992, eligibility to marketing loan benefits was restricted to upland cotton grown on acreage that was enrolled in the deficiency payment programme.

72. In sum, the United States not only “decided on whatever outlay was required to meet that rate of support”, it also took various administrative decisions that implemented the rate of support and transposed it into specific payment rates that resulted in identifiable budgetary outlays. The United States took those decisions with respect to all of the programmes including crop insurance and Step 2, as well as with respect to storage payments and interest subsidies.⁵⁵ Thus, the collective effect of these multiple decisions was to decide on the amount of expenditures for MY 1992. The only way to express this multitude of decisions and conduct the required comparison with MY 1999-2002 is to use total monetary amounts of budgetary expenditures.

(60) Can you provide information on the support decided in 1992 and the years with which you believe it should be compared, on a per support programme / per unit of production basis / per annum basis? If possible, please specify how, if at all, budget outlays may be transposed into units of production, and which units of production are best to use.

Brazil’s Comment on US Answer:

73. Brazil notes that the United States has not provided, as requested, any per support measure, per unit figures of support that it decided in 1992 and support it granted in other years. Nor did the United States provide any information whatsoever on how to account for Step 2 payments, cottonseed payments, storage payments and interest subsidies because there is no way such measures could be measured using the simplistic US rate of support only approach.

74. In addition, the United States does not respond to the Panel’s request to transpose this rate of support into budgetary outlays per pound of production. Brazil refers the Panel to paragraphs 84-85 of its Rebuttal Submission, where it provides a new chart reflecting new information provided by the United States for various programmes.⁵⁶

(61) Does the United States consider that Article 13(b)(ii) permits a comparison on any other than a per pound basis?

Brazil’s Comment on US Answer:

75. The United States admits that Article 13(b)(ii), and in particular the term “decided”, permit a comparison different from comparing a rate of support, *had the US domestic support measures been structured (i.e. decided) differently* than characterized by the United States.⁵⁷ This admission is significant, because, in fact, the US measures *were structured quite differently* from what the

⁵⁴ US 11 August Answer to Question 57, para. 113.

⁵⁵ US 11 August Answer to Question 67.

⁵⁶ US 11 August Answer to Question 67, para. 129-134.

⁵⁷ US 11 August Answer to Question 61, para. 118.

United States asserts. Professor Sumner⁵⁸ established that the US support programmes in MY 1992 did *not* provide a rate of support of 72.9 cents per pound to each pound of upland cotton produced in the United States. Numerous restrictions on the availability of the support by the deficiency payment programme and the marketing loan programme existed. In addition, participation in both programmes was costly to farmers, as farmers were mandated to set aside a certain percentage of acreage every year. USDA Chief Economist Keith J. Collins and USDA Deputy Chief Economist Joseph W. Glauber explain that

[s]everal programme changes beginning with the 1985 Farm Act reduced the ability of deficiency payments to stabilize incomes by fixing programme payment yields, reducing the amount of acreage eligible for payments, and tightening payment limits. In addition, many producers elected not to participate in farm programs, making a large portion of production not covered by payments and a large portion of producers ineligible for them by the early 1990s.⁵⁹

76. This statement confirms the existence of severe restrictions on the availability of deficiency payments and the cost of participating in the programmes. Were there no cost associated with the programme, no rational farmer would opt to not take the “free money”, *i.e.*, nearly everybody would participate. These conscious decisions by USDA and other US Government agencies must, therefore, be reflected in the claimed rate of support provided by the various non-green box domestic support measures during MY 1992.

77. Brazil agrees with the European Communities that such a *mélange* of domestic support measures decided in MY 1992 must be accounted for “in monetary terms”.⁶⁰ While the European Communities advocates using an AMS-like approach for the support decided in MY 1992,⁶¹ Brazil considers that an expenditure approach more accurately reflects the text of Article 13(b)(ii), which does not refer to AMS or “product-specific”. Brazil emphasizes that the domestic support measures that need to be included in this approach are all those domestic support measures that provide support to upland cotton.

78. Furthermore, the US “72.9 methodology” is inconsistent with the object and purpose of Article 13(b)(ii) and of the Agreement on Agriculture to correct and prevent restrictions and distortions in world agricultural markets.

79. Accepting the US interpretation that eligibility criteria and participation costs of a programme are irrelevant would enable Members like the United States to avoid the disciplines of the SCM Agreement on trade-distortive subsidies. For example, the United States in MY 1992 decided and applied restrictive support programmes that required costly land set aside programs, low payment yields, restricted payments to 85 per cent of eligible acres, tied benefits from the marketing loan programme to participation in the costly deficiency payment programs, and applied payment limitations, among others. The US interpretations would allow it in MY 2002 to lift all of these restrictions and maintain the rate of support without affecting its entitlement to peace clause exemption. The approach taken to its extreme would allow a Member that decided a rate of support of 72.9 cents per pound for 0.0001 per cent of its production in MY 1992, to provide a rate of support of 72.9 cents per pound to 100 per cent of its production in MY 2002 without affecting its entitlement to peace clause exemption. Every legitimate comparison must take account of economic realities of support regimes in MY 1992 and in later marketing years during the implementation period. And these realities show that the support increased massively.

⁵⁸ Exhibit Bra-105 (Statement of Professor Daniel Sumner at the First Meeting of the Panel).

⁵⁹ Exhibit Bra-180 (“Will Policy Changes Usher in a New Era of Increased Agricultural Market Variability?,” Keith J. Collins, Joseph W. Glauber, Choices, Second Quarter 1998, p. 28).

⁶⁰ EC Answer to Third Party Question 22, para. 47 and 49.

⁶¹ EC Answer to Third Party Question 22, para. 49.

(66) Could you please comment on the relative merits of each of the following calculation methods for purposes of the comparison of support to upland cotton with 1992, irrespective of whether a particular measure should be included or excluded:

- (a) Total budgetary outlays (Brazil's approach)**
- (b) Budgetary outlays per unit of upland cotton: Could you please calculate and provide an estimate for the marketing years 1992 and 1999-2002, respectively, and draw the Panel's attention to any factors / qualifications that the Panel would need to be aware of.**

Brazil's Comment on US Answers:

80. Brazil comments jointly on both of the 11 August Answers provided by the United States. In essence, the United States rejects any approach based on budgetary outlays as *ex post* or retrospective and as does not reflecting its alleged single decision taken during MY 1992.⁶² Based on the same argument, the United States also declines the Panel's request for information on how to calculate budgetary outlays per unit of upland cotton.⁶³ Therefore, Brazil refers the Panel to its own 11 August Answer to Question 60 and 66(b) for the only evidence in that respect as well as to Brazil's reservations concerning this approach.⁶⁴

81. The United States maintains that because its support programmes depend on a price-gap, only a rate of support approach can reflect the US decision.⁶⁵ It further maintains, that any budgetary approach would automatically reflect also producers' planting and participation decisions and market prices, factors that the United States alleges, it could not have decided.⁶⁶ However, Brazil has demonstrated that the anticipated participation in the deficiency payment and marketing loan programme was an important aspect of the decision on the acreage reduction programme. Professor Sumner has indicated that, based on historical participation data and projections about other programme parameters, the United States in MY 1992 had a very good idea of the participation rate that would result from the setting of a 10-per cent acreage reduction rate under the deficiency payment programme.

82. Further, Brazil has demonstrated above that the range of programme decisions the United States has taken, including decisions on deficiency payment rates, adjusted world prices and Step 2 payment rates in connection with decisions on other programme parameters, impacted the amount of budgetary outlays. Thus, while the United States certainly did not decide on market prices, it took a number of decisions that translated these market prices into actual expenditures for MY 1992.

83. The European Communities and other third parties to this dispute agree with Brazil that the appropriate basis for a comparison of the support decided in MY 1992 with support granted in later marketing years during the implementation period is a approach based "on monetary terms".⁶⁷ Given the special situation of the EC with respect to the peace clause decision, it may be appropriate to use an *ex ante* AMS-like approach to its decision during MY 1992 compared to the actual AMS for later marketing years.⁶⁸ But even that decision would be expressed in "monetary terms".

⁶² US 11 August Answer to Question 66, para. 119-120.

⁶³ US 11 August Answer to Question 66, para. 120.

⁶⁴ See Brazil's 11 August Answer to Question 60, para. 94-98 and Brazil's Answer to Question 66(b), para. 117-119.

⁶⁵ US 11 August Answer to Question 66, para. 119.

⁶⁶ US 11 August Answer to Question 66, para. 119.

⁶⁷ EC Answer to Third Party Question 22, para. 47.

⁶⁸ EC Answer to Third Party Question 22, para. 47-49.

84. Total expenditures for MY 1992 and total expenditures for marketing years during the implementation period are the only legitimate bases for the comparison required by Article 13(b)(ii) of the Agreement on Agriculture. All other calculation methods are either not supported by a *Vienna Convention* analysis of Article 13(b)(ii) (US rate of support approach; US rate of support approach as modified by Professor Sumner), or have major shortcomings that should lead them to be used with extreme caution (budgetary outlays per unit). Brazil notes that its expenditure approach and the analogous AMS calculation yield identical results, if one were to account for deficiency payments in terms of expenditures rather than by using the formula approach offered by Annex 3, paragraph 10-11 of the Agreement on Agriculture.⁶⁹

(d) *Per unit rate of support for upland cotton (Prof. Sumner's approach at the first session of the first substantive meeting).*

Brazil's Preliminary Comment on US Answer:

85. Brazil will further comment on any answer pursuant to the US promise to provide "a detailed critique of Mr. Sumner's analysis."⁷⁰ As for the 11 August US comments, Brazil has earlier in its 22 August Comments to Questions 66(a) and (b) argued that Professor Sumner properly accounted for all US decisions.⁷¹ Concerning the inclusion of crop insurance subsidies, PFC and market loss assistance payments, as well as direct and counter-cyclical payments, Brazil has demonstrated in its Rebuttal Submission⁷² and in comments to Questions 38 and 43 that these domestic support measures constitute support to upland cotton as well as product-specific support. Thus, there is no basis to exclude these payments from any US calculation of upland cotton AMS.

(67) The Panel requests the parties to calculate and submit estimates of the AMS for upland cotton for marketing years 1992, 1999, 2000, 2001 and 2002. For this purpose the parties are each requested to submit AMS calculations for upland cotton (using the budgetary-outlay/non-price gap methodology employed by the United States in respect of cotton in its DS Notifications (e.g., G/AG/N/USA/43) and using the formats and supporting tables in document G/AG/2) on the same basis as would be the case in calculating a product specific AMS for the purposes of the calculation of the "Total Current AMS" in any year in accordance with the relevant provisions, including as appropriate Article 1(a), (b) and (h), Article 6 and Annex 3 to the Agreement.

Brazil's Comment on US Answers:

86. The United States' calculation of upland cotton AMS is incomplete because it does not account for the product-specific support provided to upland cotton from PFC and market loss assistance payment, direct and counter-cyclical payments and crop insurance subsidies. Brazil has discussed the nature of these programs as product-specific (and as constituting "support to upland cotton") and the incorrect US interpretation of "product-specific" elsewhere.⁷³ Brazil further notes that the United States has included in its calculation of upland cotton AMS storage payments and interest subsidies – product-specific support measures that the United States has not mentioned so far during this dispute.⁷⁴ Based on this and other new data supplied by the United States, Brazil provides an update of its AMS calculation and of its analysis of total budgetary outlays.⁷⁵

⁶⁹ Brazil's 11 August Answer to Question 60, para. 97, and to Question 67, para. 130.

⁷⁰ US 11 August Answer to Question 66, para. 121.

⁷¹ See para. 81-85 *supra*.

⁷² Rebuttal Submission of Brazil, paras. 24-67.

⁷³ Rebuttal Submission of Brazil, para. 13-67.

⁷⁴ Brazil notes that it has asked the United States in consultations for information on any other domestic support measures that provides support to upland cotton and that the United States did not mention these

III. EXPORT CREDIT GUARANTEES

- 71 (a) Is an export credit guarantee a financial contribution in the form of a "potential direct transfer of funds or liabilities (e.g. loan guarantee)" within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement? Why or why not? Does it confer a benefit within the meaning of Article 1.1(b)? Why or why not? If so, to whom?
- (b) How, if at all, would these elements be relevant to the claims of Brazil, and the United States response thereto?

87. In responding to this Question, the United States relies solely on Article 10.2 of the Agreement on Agriculture and – alternatively – restricts the use of context from the SCM Agreement to item (j) only.⁷⁶ Brazil addresses the United States' arguments regarding Article 10.2 of the Agreement on Agriculture at paragraphs 99-100 of its Rebuttal Submission. In determining what constitutes an export subsidy within the meaning of Article 10.1 of the Agreement on Agriculture, Brazil considers that the Panel should refer to Articles 1(e) and 10.1 of the Agreement on Agriculture itself, as well as to contextual guidance included in Articles 1 and 3 of the SCM Agreement, and in item (j) of the Illustrative List of Export Subsidies annexed to the SCM Agreement. This is consistent with the Appellate Body's decisions in *US – FSC*⁷⁷ and *Canada – Dairy*.⁷⁸

(73) The Panel could arguably take the view that Articles 1 and 3 of the SCM Agreement were relevant in assessing the WTO-consistency of United States export credit guarantees. The United States has yet to submit any evidence or argumentation on this point, either as potential context for interpretation of the terms in Article 10 of the Agreement on Agriculture or in relation to Brazil's claims under the SCM Agreement. The Panel would therefore appreciate United States views in respect of this situation, and invites the United States to submit relevant argumentation and evidence.

Brazil's Comment on US Answer:

88. The United States argues that it does not need to address Articles 1 and 3 of the SCM Agreement because it "does not believe that Brazil has submitted evidence and argumentation that would establish a *prima facie* case in favour of Brazil's claims . . ." ⁷⁹ Since the United States has surpassed its quantitative export quantity reduction commitment levels, Article 10.3 of the Agreement on Agriculture allocates the burden to the United States to prove that its excess exports did not benefit from export subsidies, including export credit guarantees.⁸⁰ Therefore, it is not Brazil, but the United States, that is faced with satisfying the elements of a *prima facie* case in favour of its defence.

(74) If the Panel decides to refer to provisions of the SCM Agreement for contextual guidance in the interpretation of the terms in Article 10 of the Agreement on Agriculture, should the Panel refer to item (j) or Articles 1 and 3 of the SCM Agreement or both?

programs during consultations. *See* Exhibit Bra-101 (Brazil's Questions for the Purposes of the Consultations, 22 November 2002, Questions 15.1-15.6).

⁷⁵ Rebuttal Submission of Brazil, paras. 73-74.

⁷⁶ US 11 August Answer to Question 71, para. 137-139.

⁷⁷ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 136-140.

⁷⁸ Appellate Body Report, *Canada – Dairy*, WT/DS103/AB/R and WT/DS113/AB/R, para. 87-90.

⁷⁹ US 11 August Answer to Question 73, para. 140.

⁸⁰ *See* First Submission of Brazil, paras. 263-268.

Brazil's Comment on US Answer:

89. In paragraph 141 of its 11 August Answer to Question 74 (and again in paragraphs 189 and 195 of its 11 August Answers to Questions 88(b) and (d), respectively), the United States asserts that "Brazil has not contested that challenged US export credit guarantee programs are within the scope of Article 10.2." The United States is incorrect. While it is possible that GSM 102, GSM 103 and SCGP export credit guarantees might be included in any international agreement that Members might some day reach in negotiations pursuant to Article 10.2 of the Agreement on Agriculture, no one knows at this stage what the scope of that agreement, if any, will be. The agreement might only cover export credits other than guarantees, like the OECD Arrangement on Guidelines for Officially Supported Export Credits, which does not cover export credit guarantees.

90. In any event, the relevant question is not whether export credit guarantees are "covered" by Article 10.2, but whether they are "exempted" by Article 10.2 from the general export subsidy disciplines of the Agreement on Agriculture. Brazil's position is that Article 10.2 does not exempt export credits like export credit guarantees from the general export subsidy disciplines of the Agreement on Agriculture, including Article 10.1 thereof. If those export credit guarantees constitute export subsidies, then they are subject to those disciplines. (In paragraph 142 of its 11 August Answer, the United States appears to concede this point, when it acknowledges that "[t]o determine the applicability of Article 10.1 to a particular measure not described in Article 9.1 first requires a determination whether a subsidy exists.")

(75) (identical to Third Party Question 32)

The Panel's attention has been drawn to Article 14(c) of the SCM Agreement (see third party submission of Canada) and to the panel report in DS 222 Canada- Export Credits and Loan Guarantees. How and to what extent are Article 14(c) of the SCM Agreement, and the cited panel report, relevant to the issue of whether or not the United States export credit guarantee programmes confer a "benefit"? What would the appropriate market benchmark be to use for any comparison? Please cite any other relevant material.

(Third Party Question 33)

What is the relevant (if any) of Brazil's statement that: "... export credit guarantees for exports of agricultural products [sic] are not available on the marketplace by commercial lenders."

Brazil's Comment on EC Answers on Third Party Question 32 (identical to Question 75) and 33 and on US Answer to Question 75:

91. The United States argues that item (j) alone is relevant context for a determination whether CCC export credit guarantee programmes are export subsidies.⁸¹ The European Communities argues that the fact that a particular financing instrument offered by a government (such as CCC guarantees) is not available on the marketplace does not mean that such financing confers a benefit *per se* within the meaning of Article 1.1(b) of the SCM Agreement.⁸² The European Communities maintain that in circumstances in which a comparable type of financing is not available on the marketplace, an "alternative" benchmark such as item (j) has to be used for determining whether a benefit exists.⁸³ While Brazil agrees with the European Communities that item (j) is an *alternative* test for the existence of an export subsidy, Brazil strongly disagrees that Article 1.1 of the SCM Agreement is – as the European Communities effectively and the United States explicitly argues – inapplicable in

⁸¹ US 11 August Answer to Question 75, para. 143.

⁸² EC's Answers to Third Party Questions, para. 68.

⁸³ EC's Answer to Third Party 35, para. 67.

such situations. Article 1.1 defines the existence of a subsidy for the purposes of the SCM Agreement and provides relevant context for the interpretation of the term “export subsidy” under the Agreement on Agriculture. Article 1.1(b) requires a comparison between what the recipient of a financial contribution received from the government and what the recipient could have received on the marketplace.⁸⁴ The Appellate Body clarified that the standard under Article 1.1(b) is not the cost incurred by the government (as under item (j)).⁸⁵ The relevant standard is the “benefit to the recipient” standard.

92. This definition of a subsidy cannot simply be read out of the SCM Agreement in a situation where there is no comparable commercial financing available. Nothing suggests that Article 1.1(b) is inapplicable in such a situation. The United States and the European Communities would certainly agree that a direct transfer of funds without consideration is not commercially available. In these circumstances, a benefit within the meaning of Article 1.1(b) of the SCM Agreement is conferred. A similar situation exists with respect to CCC guarantees. A recipient of CCC guarantees cannot receive a similar financial contribution on commercial terms, as no such financing is available on the marketplace.⁸⁶ Thus, the CCC export credit guarantee programmes confer benefits. Brazil notes that the United States agreed, in its third party submission in *Canada – Aircraft II*, that where there is no comparable financial product on the market, a programme confers benefits *per se*.⁸⁷

(76) How does the United States respond to Brazil’s statement that : “...export credit guarantees for exports of agricultural exports [sic] are not available on the marketplace by commercial lenders.”?

Brazil’s Comment on US Answer:

93. The United States asserts that export credit insurance may be a comparable commercial product to CCC export credit guarantees.⁸⁸ As noted in paragraph 103-104 of Brazil’s Rebuttal Submission, the United States acknowledges that there are distinctions between insurance coverage and guarantees. Thus, the terms of insurance coverage by private, market-based financial institutions cannot serve as a benchmark against which to determine whether the CCC guarantee programmes confer “benefits,” within the meaning of Article 1.1(b) of the SCM Agreement. As the United States has elsewhere noted, “[i]f the commercial market does not offer a particular borrower the *exact terms* offered by a government, then the government is providing a benefit to the recipient whenever those terms are more favourable than the terms that are available in the market.”⁸⁹ Moreover, the United States has not provided actual terms for insurance coverage by private, market-based financial institutions. Brazil understands that private, market-based insurance coverage for agricultural products is not available for periods extending nearly as long as periods provided by CCC guarantees.

(77) How does the United States interpretation of "long term operating costs and losses" in item (j) as claims paid give meaning to both "costs" and "losses"? Do claims paid represent "losses" or "costs" or both? If claims paid is represented by "losses", what would go into the "cost" element of item (j)? Could the United States expand on why it disagrees with the items which Brazil identifies for inclusion in the examination to be conducted under item (j)?

⁸⁴ Appellate Body, *Canada – Aircraft*, WT/DS70/AB/R, para. 157.

⁸⁵ Appellate Body, *Canada – Aircraft*, WT/DS70/AB/R, para. 160.

⁸⁶ See also Rebuttal Submission of Brazil, paras. 103-105.

⁸⁷ Panel Report, *Canada – Aircraft II*, WT/DS222/R, Annex C-2 (para. 7). See also Answers to Questions by Brazil, para. 151.

⁸⁸ US 11 August Answer to Question 76, para. 144.

⁸⁹ Panel Report, *Canada – Aircraft II*, WT/DS222/R, Annex C-2 (para. 7).

Brazil's Comment on US Answer:

94. In paragraph 145 of its response, the United States suggests that claims and defaults must exceed "revenue from whatever source it may be derived" to meet the elements of item (j), despite the fact that item (j) limits the revenue to be used to offset operating costs and losses to "premium rates". On the other hand, the United States maintains that it is only legitimate to account for claims and defaults in the context of item (j), and not for other operating costs and losses such as interest on debt to Treasury⁹⁰, even though those sorts of other costs and losses are covered by the ordinary meaning of the terms included in item (j).⁹¹ This is incongruous, and not supported by the text of item (j).

95. Further, Brazil refers the Panel to its Rebuttal Submission and to its 22 August Comments to the US Answers to Question 81 below for a more detailed discussion on the elements that are to be included in an item (j) analysis.

(78) Can the United States provide supporting documentation for data used relating to "costs and losses" in paragraph 173? Could the United States confirm that the figures cited in paragraph 173 of its first written submission relate to the SCGP? Why did the United States cite these figures after stating that it is not possible to make any assessment of the long-term operating costs and losses of this programme?

Brazil's Comment on US Answer:

96. The United States has failed to provide the supporting documentation requested by the Panel. The data mentioned in paragraph 149 of the United States' 11 August Answer could have been provided for review and analysis by the Panel and Brazil. As a result, Brazil requests that the Panel reject the United States' assertions in paragraph 173 of the US First Submission.

(80) (identical to Third Party Question 35)

Did the drafters of the Agreement on Agriculture include export credit guarantees in Article 9.1 of the Agreement on Agriculture? Why or why not?

Brazil's Comment on EC Answer:

97. Brazil agrees with the European Communities that "Article 9.1 represents a list of export subsidies ... that are subject to reduction commitments."⁹² Export credit guarantees are not included, as they do not constitute *per se* export subsidies subject to reduction commitments. Only if export credit guarantees confer a benefit within the meaning of Article 1.1(b) and/or Article 14(c) of the SCM Agreement, or if they are provided at premium rates that are inadequate to cover the long-term operating costs and losses of the export credit guarantee programme, do they constitute export subsidies to be assessed against the export subsidy reduction commitments of a Member. In these circumstances, export credit guarantees must not be provided in a manner inconsistent with Article 10.1 of the Agreement on Agriculture.

98. Because export credit guarantees are not – under a *Vienna Convention* interpretation of Article 10.2 of the Agreement on Agriculture – excluded from the general export subsidy disciplines in AoA Article 10.1, their provision counts towards the export subsidy reduction commitments of a Member. Article 10.2 states that after agreement on disciplines governing the provision of export credits is reached, these credits can only be provided in conformity therewith. Brazil does not want to speculate on whether the internationally-agreed disciplines will subject export credit guarantees to

⁹⁰ First Submission of the United States, para. 178.

⁹¹ See Oral Statement of Brazil, para. 123.

⁹² EC's Answers to Third Party Questions 35, para. 70.

reduction commitments. In any event, under the current regime governing the provision of export credit guarantees, they are subject to the anti-circumvention disciplines in Article 10.1 of the Agreement on Agriculture and count towards a Member's export subsidy reduction commitments, if they constitute export subsidies within the meaning of the Agreement on Agriculture (and, by context, the SCM Agreement).

(81) How does the United States respond to the following in Brazil's oral statement

(a) paragraph 122 (rescheduled guarantees)

Brazil's Comment on US Answer:

99. Although "rescheduled amounts are counted as *receivables*, not losses," that does not mean that rescheduled amounts are actually collected, or even expected to be collected. CCC's 2002 financial statements demonstrate that many of CCC receivables are classified as "uncollectible" – in fact, \$3.34 billion of total receivables of \$6.93 billion are classified as "uncollectible."⁹³ Moreover, as noted in Brazil's 11 August Comment on Question 77 (at paragraph 162), the US General Accounting Office has stated that historically, the majority of GSM support that is rescheduled is "in arrears".⁹⁴ Based on this evidence, it is simply not accurate for the United States to argue, in paragraph 155 of its 11 August Answer, that "[t]he history of rescheduled Commodity Credit Corporation (CCC) export credit guarantee claims over the long-term (the 10-year period 1993-2002) confirms" that "the United States does in fact collect on the rescheduling."

100. Brazil also notes that the United States has not provided any documentary evidence that would support its assertion.

(c) paragraphs 125 ff. (guaranteed loan subsidy)

Brazil's Comment on US Answer:

101. In paragraphs 108-110 of its Rebuttal Submission, Brazil summarizes the several bases on which the Panel can rest a finding that the GSM 102, GSM 103 and SCGP programmes constitute export subsidies under item (j). The United States criticizes one of those bases – the FCRA cost formula – as inappropriate because it allegedly relies on "estimated" rather than "actual" data about the costs of the programmes.⁹⁵ This appears to be the United States' sole defence, which Brazil again notes applies only to the FCRA cost formula and not the other evidence and bases summarized by Brazil in paragraphs 108-110 of its Rebuttal Submission. In any event, Brazil rebuts the US arguments concerning "estimated" versus "actual" data in paragraphs 111-119 of its Rebuttal Submission, and asks the Panel to refer to Brazil's arguments therein.

⁹³ Exhibit Bra-158 (US Department of Agriculture, Office of Inspector General, Financial and IT Operations, Audit Report, *Commodity Credit Corporation's Financial Statements for Fiscal Year 2002*, Audit Report No. 06401-15-FM (December 2002), Notes to the Financial Statements, p. 14).

⁹⁴ Exhibit Bra-152 (GAO, Statement of Allan I. Mendelowitz, Director, Trade, Energy and Finance Issues, National Security and International Affairs Division, before the Task Force on Urgent Fiscal Issues of the Committee on Budget of the US House of Representatives, *Status Report on GAO's Reviews of the Targeted Export Assistance Programme, the Export Enhancement Programme, and the GSM-102/103 Export Credit Guarantee Programmes*, GAO/T-NSIAD-90-53, 28 June 1990, p. 14). See also Exhibit Bra-181 (US General Accounting Office, Report to the Ranking Minority Member, Committee on Agriculture, Nutrition, and Forestry, US Senate, *Former Soviet Union: Creditworthiness of Successor States and US Export Credit Guarantees*, GAO/GGD-95-60 (February 1995), p. 50-52 (demonstrating that most of the rescheduled Russian and Former Soviet Union GSM claims have been in arrears)).

⁹⁵ See US 11 August Answers to Questions, paras. 157-161, 162-163, 169-172, 173.

102. Brazil notes that the United States has offered no documentation and data to support the figures included in paragraph 160 of its 11 August Answer. The Panel should not accept these unsupported assertions by the United States.

103. At paragraphs 122-123 of its 11 August Answer to Question 81(c), the United States asserts that “[a] cohort consists of all transactions associated with each type of guarantee issued during a particular year”, and that “[n]ot until the cohort is closed can one make an assessment as to whether or not that particular cohort represents a cost to the Federal Government”. Brazil notes that a “cohort” is not necessarily composed of *all* guarantees issued in a particular year. As the US Office of Management and Budget notes, cohorts may also be divided according to risk categories, with annual reestimates calculated according to those risk category-based cohorts.⁹⁶ The United States in fact acknowledges at paragraph 148 of its 11 August Answer to Question 86 that “[a]ll countries eligible for any of the CCC export credit guarantee programmes are categorized according to risk”.

(d) paragraphs 127-129 (re -estimates, etc.)

Brazil’s Comment on US Answer:

104. In paragraph 163 of its 11 August Answer, the United States asserts that the “net total for all cohorts for guarantees issued since 1992 currently stands at a downward re-estimate of \$1.9 billion”, suggesting that by the time a cohort is closed and final data becomes available, the cohort becomes profitable. Although the United States offers no citation, the \$1.9 billion lifetime reestimate figure appears to be taken from the Federal Credit Supplement attached to the 2004 US budget. As discussed further in paragraphs 115-117 of Brazil’s Rebuttal Submission, however, the United States fails to note that when these total lifetime reestimates for all cohorts of guarantees disbursed since 1992 are netted against the total *original* subsidy estimates adopted each budget year during the period 1992-2002, *the resulting loss is nearly \$1.75 billion.*

(b) paragraph 123 (interest on debt to Treasury)

Brazil’s Comment on US Answer:

105. The United States’ 11 August Answer addresses interest rate reestimates under the FCRA cost formula. Paragraph 123 of Brazil’s Statement at the First Panel Meeting, however, to which the Panel’s question refers, does not address the treatment of interest paid by the CCC to the Treasury Department under the FCRA cost formula. Rather, in paragraph 123 of its Oral Statement at the First Meeting of the Panel, Brazil was responding to the US assertion that *Brazil’s constructed formula* for determining whether the CCC guarantee programmes’ operating costs and losses outpaced premiums collected should not have included interest paid by the CCC to the Treasury Department. In paragraph 123 of its Oral Statement, Brazil argued that under the ordinary meaning of the term “operating costs”, interest paid by the CCC to the Treasury Department should be included in an assessment of the programmes under item (j). Brazil’s arguments have nothing to do with interest rate reestimates under the FCRA cost formula. The United States’ answer is, therefore, only relevant in so far as the United States now seems to acknowledge that, for the purposes of Brazil’s revised constructed formula, interest payments to Treasury are properly included.⁹⁷

⁹⁶ Exhibit Bra-116 (OMB Circular A-11, p. 185-16 – 185-17).

⁹⁷ US 11 August Answer to Question 81(b), para. 167.

(e) Exhibits BRA-125-127

Brazil's Comment on US Answer:

106. The United States' 11 August Answer is incorrect. Reestimates are recorded in the "programme account" segment of the CCC guarantee programme budget, in line item 00.07 (interest on reestimates is recorded in line 00.08).⁹⁸ Furthermore, Brazil has consistently also included the financing account in its exhibits, including – contrary to the US allegation⁹⁹ – in Exhibit Bra-127.

(f) the chart on page 53 of Brazil's oral statement at the first session of the first Panel meeting relating to "Guaranteed Loan Subsidy and Administrative Expenses of US Export Credit Guarantee Programmes GSM-102 GSM 103 and SCGP"?

Brazil's Comment on US Answer:

107. Brazil refers the Panel to paragraphs 111-119 of Brazil's Rebuttal Submission for discussion of the US arguments concerning "estimated" versus "actual" data.

(g) In respect of (a)-(f) above, how and to what extent do the information and data presented for the export guarantee programmes concerning "programme" and "financing", "summary of loan levels", "subsidy budget authority", "outlay levels", etc., in particular in Exhibits BRA-125-127, reflect "actual costs and losses" of the GSM-102, GSM-102 and SCGP export credit guarantee programmes(see e.g. Brazil's closing oral statement at the first session of the first substantive meeting, paragraph 24)?

Brazil's Comment on US Answer:

108. Brazil refers the Panel to paragraphs 111-119 of Brazil's Rebuttal Submission for discussion of the US arguments concerning "estimated" versus "actual" data.

(84) Is the Panel correct in understanding that, under the GSM-102 and GSM-103 programmes, the exporter pays a fee calculated on the dollar amount guaranteed, based on a schedule of rates applicable to different credit periods? How and on what basis are the fee rates fixed? Do the fee rates ever change? If so, how and for what reason? Would it be necessary to amend the legislation and/or regulations in order to adjust the fee rates?

Brazil's Comment on US Answer:

109. As noted in Brazil's 11 August Comment on Question 84 (at paragraphs 192-194), GSM 102 and GSM 103 fees are charged according to a fee schedule that does not account for the country risk involved or the credit rating of the borrower. The US Department of Agriculture's Office of the Inspector General noted in June 2001 that "the fees CCC charges for its GSM-102 and GSM-103 export credit guarantee programmes have not been changed in 7 years and may not be reflecting current costs".¹⁰⁰ It repeated this statement in February 2002.¹⁰¹

⁹⁸ See Exhibits Bra-88 to Bra-95 (US budgets for the years 1996-2003); Exhibits Bra-125 to Bra-127 (US budgets for the years 1994, 1995 and 2004). See also Exhibit Bra-184 (US budget for fiscal year 1993); Exhibit Bra-183 (US budget for fiscal year 1992).

⁹⁹ US 11 August Answer to Question 81(e), para. 168.

¹⁰⁰ Exhibit Bra-153 (US Department of Agriculture Office of Inspector General Financial and IT Operations Audit Report of the Commodity Credit Corporation's Financial Statements for Fiscal Year 2000, Audit Report No. 06401-14-FM (June 2001), p. 31).

110. Moreover, the US General Accounting Office (“GAO”) analyzed CCC’s failure to charge guarantee fees that take account of country risk or the creditworthiness of individual borrowers. Brazil quotes at length from the GAO study, since it provides further corroborating evidence that beneficiaries of CCC guarantees receive terms better than available on the market, and that CCC guarantee fees do not cover the costs of the CCC guarantee programmes:

Although GSM-102 recipient countries vary significantly from one another in terms of their risk of defaulting on GSM-102 loans, CCC does not adjust the fee that it charges for credit guarantees to take account of country risk. CCC fees are based upon the length of the credit period and the number of principal payments to be made. For example, for a 3-year GSM-102 loan with semiannual principal payments, CCC charges a fee of 55.6 cents per \$100, or 0.56 per cent of the covered amount. For 3-year loans with annual principal payments, the fee is 66.3 cents per \$100.¹⁰¹ CCC fees that included a risk-based component might not cover all of the country risk, but they could help to offset the cost of loan defaults.

USDA officials told us that including a fee for country risk could reduce the competitiveness of GSM-102 exports. However, they said they did not have recent or current data to support their claim.

The US Export-Import Bank, which provides credit guarantees to promote a variety of US exports, uses risk-based fees to defray the cost of defaults on its portfolio. Under its system, each borrower/guarantor is rated in one of eight country risk categories. Exposure fees vary based on both the level of assessed risk and the length of time provided for repayment. For example, in the case of repayment over 3 years, a country rated in the lowest risk category is charged a fee of 75 cents per \$100, whereas a country in the highest risk category is charged a fee of \$5.70 per \$100 of coverage. Thus, the bank’s fee structure includes a substantial added charge for high country risk. According to the bank, its system is designed to remain as competitive as possible with fees charged by official export credit agencies of other countries.

Under section 211(b)(1)(b) of the 1990 Farm Bill, CCC is currently restricted from charging an origination fee for any GSM-102 credit guarantee in excess of an amount equal to 1 per cent of the amount of credit extended under the transaction.¹⁰² This restriction was initially enacted in 1985 following proposed administration legislation to charge a 5-per cent user fee for exports backed with credit guarantees. Some Members of Congress were concerned that such a fee would adversely affect the competitiveness of GSM-102 exports. Under the 1-per cent restriction, CCC would be considerably limited in the size of the fee that it could charge to take account of country risk should it decide to do so. For example, as previously noted, CCC charges 0.56 per cent for a loan payable in 3 years and with principal payments due annually. The most it could increase the fee would be 0.44 per cent. In contrast, the Export-Import Bank currently charges fees as high as 5.7 per cent for 3-year loans.¹⁰³

¹⁰¹ Exhibit Bra-154 (US Department of Agriculture Office of Inspector General Great Plains Region Audit Report of the Commodity Credit Corporation’s Financial Statements for Fiscal Year 2001, Audit Report No. 06401-4-KC (February 2002), p. 49 (“[T]he fees CCC charged for its GSM-102 and GSM-103 export credit guarantee programs have not been changed for many years and may not be reflecting current costs.”).

¹⁰² The United States confirmed in paragraphs 179-180 of its 11 August Answer that this remains the case.

¹⁰³ Exhibit Bra-181 (US General Accounting Office, Report to the Ranking Minority Member, Committee on Agriculture, Nutrition, and Forestry, US Senate, *Former Soviet Union: Creditworthiness of Successor States and US Export Credit Guarantees*, GAO/GGD-95-60 (February 1995), p. 135-136). Although government support from the Export-Import Bank does not constitute a market benchmark for the purposes of

111. Brazil notes that CCC fees for GSM 102 have not changed materially since the GAO published its report in 1995.¹⁰⁴ Moreover, the United States confirmed in its 11 August Answer to Question 84 (at paragraph 180) that US law prohibits CCC from charging fees in excess of one per cent of the guaranteed dollar value of the transaction.

(85) Is the Panel correct in understanding that, under the SCGP, the exporter pays a fee for the guarantee calculated on the guaranteed portion of the value of the export sales? How and on what basis are the fee rates fixed? Do the fee rates ever change? If so, how and for what reason? Would it be necessary to amend the legislation and/or regulations in order to adjust the fee rates? Please explain any "risk" assessment involved in the programme .

Brazil's Comment on US Answer:

112. As noted in Brazil's 11 August Comment on Question 85 (at paragraph 195), SCGP fees do not vary according to the country risk involved or the credit rating of the borrower. With or without the "risk sharing" described in paragraph 183 of the United States' 11 August Answer, Brazil notes the United States' acknowledgement that "CCC does not determine the creditworthiness of importers participating in the SCGP."¹⁰⁵ This presents further corroborating evidence that beneficiaries of CCC guarantees receive terms better than available on the market, and that CCC guarantee fees do not cover the costs of the CCC guarantee programmes.

(86) Is there a risk categorization in relation to three export credit guarantee programmes (GSM-102, GSM-103 and SCGP)? Does this have any impact on premiums payable and the ability of the CCC to on-sell the guarantees ?

Brazil's Comment on US Answer:

113. Brazil notes the United States' acknowledgement that "[a] country's risk classification has no impact on the premiums payable under the US export credit guarantee programmes". CCC's failure to account for country risk provides further corroborating evidence that beneficiaries of CCC guarantees receive terms better than available on the market, and that CCC guarantee fees do not cover the costs of the CCC guarantee programmes.

(87) What proportion of CCC (export-related and total) long term operating costs and losses are represented by GSM-102, GSM-103 and SCGP programmes?

Brazil's Comment on US Answer:

114. The United States asserts that funding for the CCC export guarantee programs is provided from the US Treasury, and is not "financed out of" the CCC. This suggests that the CCC export guarantee programs are not self-sustaining. This suggests in turn that the CCC export guarantee programmes meet the elements of item (j) and, thus, constitute export subsidies.

(88a) Is the Panel correct in understanding that the United States' argument is that, at present, by virtue of Article 10.2 of the Agreement on Agriculture, there are no disciplines on agricultural export credit guarantees under the Agreement on Agriculture (or the SCM Agreement)?

Article 1.1(b) of the SCM Agreement, Brazil offers this example to demonstrate that the CCC guarantee programs do not even meet *non-market* benchmarks.

¹⁰⁴ Brazil's 11 August Answer to Question 77 and 84, para. 167, 193-194.

¹⁰⁵ US 11 August Answer to Question 85, para. 138.

Brazil's Comment on US Answer:

115. The United States incorrectly argues, in paragraph 187 of its 11 August Answer, that “[i]f export credit guarantee programmes were already subject to export subsidy disciplines, then Article 10.2 would be unnecessary.” The negotiators may have considered it useful to negotiate additional disciplines for export credit guarantees one day, but that does not mean that they intended for export credits to be exempted from the general disciplines of the Agreement on Agriculture while those negotiations were pending.

116. The United States also argues in paragraph 187 that Brazil's use of the term “specific” disciplines somehow defeats Brazil's interpretation of Article 10.2. Brazil uses the term “specific” disciplines merely as a way of distinguishing between one actual and one potential category of export subsidy disciplines under the Agreement on Agriculture: (i) those “general” disciplines that apply to export credit guarantees today; and (ii) those “specific” disciplines that would additionally apply to export credits upon the completion of the negotiations called for by Article 10.2.

(b) Does the United States agree with the following proposition: a WTO Member may therefore extend agricultural export credit guarantees without charging a premium, and for an indefinite period, in addition to any other terms and conditions it may wish? How would this reconcile with the title of Article 10 of the Agreement on Agriculture ("Prevention of Circumvention on Export Subsidy Commitments"), and with other commitments contained in the Agreement on Agriculture? Please cite any relevant material, including any past WTO dispute settlement cases. How would this reconcile with the United States' own statement, at paragraph 21 of its closing oral statement that "of course, the United States may not provide subsidies without any limit".

Brazil's Comment on US Answer:

117. Please see Brazil's 22 August Comment on the United States' 11 August Answer to Question 74 for observations on the United States' assertion, in paragraph 189, that “Brazil has not contested that US export credit guarantee programmes are encompassed by the terms of Article 10.2.”

118. The United States argues that an interpretation of Article 10.2 of the Agreement on Agriculture that exempts export credits from the general export subsidy disciplines of that agreement is consistent with the title of Article 10 – “Prevention of Circumvention of Export Subsidy Commitments.”¹⁰⁶ The United States' argument is absurd. Since negotiations on specific disciplines pursuant to Article 10.2 have not been concluded, the United States' interpretation of Article 10.2 would leave export credit support completely undisciplined, and open to the abuse outlined in the text of the Panel's question. In this way, the United States' interpretation of Article 10.2 *facilitates*, rather than *prevents*, circumvention of its export subsidy commitments.

119. The United States also argues that the portion of Article 10.2 calling for Members to work toward the negotiation of specific disciplines on export credits also contributes to the prevention of circumvention. As the ordinary meaning of the first portion of Article 10.2 demonstrates, however¹⁰⁷, Members are not even required to actually negotiate specific disciplines for export credits, let alone to reach actual agreement on those specific disciplines. All Members have agreed to do is to work toward the development of those specific disciplines, which does not in itself prevent circumvention.

(c) If, as the United States argues, there are no disciplines on export credit guarantees in the Agreement on Agriculture, how could export credit guarantees

¹⁰⁶ US 11 August Answer to Question 88(b), para. 190.

¹⁰⁷ See Oral Statement of Brazil, para. 102.

"conform fully to the provisions of Part V" of the Agreement on Agriculture within the meaning of Article 13 (how can you assess "conformity" or non-conformity when there are allegedly no disciplines against which such an assessment could occur)?

Brazil's Comment on US Answer:

120. The United States argues that since export credit guarantees are not subject to export subsidy disciplines in the Agreement on Agriculture, they "cannot be out of compliance with Part V" of the that agreement. The pertinent question is whether export credit guarantees can, under the terms of Article 13(c), "conform fully to the provisions of Part V" of the Agreement on Agriculture. In this regard, the United States ignores the conclusions of the panel in *Canada – Aircraft (21.5)*.¹⁰⁸ As noted in Brazil's 11 August Comment on Question 88(c) (paragraphs 200-202), if the United States is correct that CCC export credit guarantees are not subject to the disciplines in Part V of the Agreement on Agriculture, then CCC guarantees cannot logically "conform fully to the provisions of Part V" and trigger the exemption from action provided for in Article 13(c).

121. Alternatively, the United States suggests that Article 13(c) does not apply to export credit guarantees because "export credit guarantees are not export subsidies within the meaning of either Article 9.1 or 10.1" of the Agreement on Agriculture. This assertion is not supported by the United States with any reference to the tools of interpretation included in the *Vienna Convention*, and is fundamentally incorrect. Brazil has demonstrated that the GSM 102, GSM 103 and SCGP export credit guarantee programs administered by the CCC constitute export subsidies within the meaning of Articles 10.1, 1(e) and 8 of the Agriculture Agreement, Article 3.1(a) of the SCM Agreement, and item (j) of the Illustrative List of Export Subsidies attached as Annex I to the SCM Agreement.¹⁰⁹

- (d) Is the United States advocating the view that its own export credit guarantee programmes, which pre-dated the Uruguay Round, are effectively "grandfathered" so as to benefit from some sort of exemption from the export subsidy disciplines of the Agreement on Agriculture? How, if at all, is it relevant that the SCGP did not, according to the United States, become relevant for upland cotton until the late 1990's (i.e. after the entry into force of the WTO Agreement)?**

Brazil's Comment on US Answer:

122. Please see Brazil's comment on the United States' 11 August Answer to Question 74 for observations on the US assertion in paragraph 189 that "Brazil has not contested that SCGP provides export credit guarantees within the meaning of Article 10.2."

IV. STEP 2 PAYMENTS

(92) Does the United States confirm that Exhibit Bra.65 represents a sample contract for exporters of eligible upland cotton to conclude with the CCC under the FSRI 2002, and that an application form (Exhibit Bra-66) needs to be filled out with data on weekly exports and submitted to the USDA FAS. Is Exhibit Bra-66- Form CCC 1045-2 also a valid example? If not, please identify any differences or distinctions.

(96) Is a domestic sale a "use" for the purposes of Step 2 payments? Is a sale for export, or export, considered a "use"?

¹⁰⁸ Panel Report, *Canada – Aircraft (21.5)*, WT/DS70/RW, para. 5.143-5.145.

¹⁰⁹ First Submission of Brazil, para. 271-294; Oral Statement of Brazil, para. 116-133; Brazil's 11 August Answers to Questions, para. 139-168, 175-189 and 192-199.

Brazil's Comments to the US Answers:

123. Brazil notes that the Step 2 regulations make a clear distinction between “domestic *users*” and “exporters”.¹¹⁰ “Domestic *users*” may only receive payment upon “proof of purchase and consumption of eligible cotton by the domestic user. . .”.¹¹¹ The agreement for domestic users provides that a domestic user is a person regularly engaged in manufacturing eligible upland cotton into cotton products in the United States and that “in the event that the cotton is not used for that purpose, the payment received shall be returned immediately and with interest”.¹¹² There is no requirement that “exporters” prove, prior to receiving payment, that exported US upland cotton be “used” for anything upon export. Rather, the payment is a function of “proof of export of eligible cotton by the exporter”.¹¹³ Thus, the structure of the Step 2 programme clearly differentiates between “export” and “use”. Article 3.1(b) applies the phrase “contingent upon *use*.” Article 3.1(a) uses the phrase “contingent . . . upon export performance”.

124. In relation to Exhibit US-21, Brazil agrees with the United States that the two different forms that have to be annexed to the User/Exporter Agreement have different objectives depending on the final destination of upland cotton. That is, if the upland cotton is *used* domestically, then the CCC-1045UP-1 form has to be completed and annexed to the User/Exporter Agreement. If the cotton is exported, then the CCC-1045UP-2 form has to be used. However, contrary to the US statement at paragraph 201 of its 11 August Answer to Question 92, the latter makes no reference whatsoever to an “Exporter User.” Indeed, the term “exporter user” is not contained either in the Step 2 regulations nor in the form that has to be annexed to the User/Exporter Agreement if the upland cotton will be exported. This is consistent with the fact that an exporter is not a “user” under the Step 2 programme and the act of exporting is unlikely a final “use” of upland cotton. In sum, Step 2 export payments are not made contingent upon “use,” but contingent upon “*export*”.

(93) Please elaborate why the United States deems that Step 2 payments upon submission of proof of export are not subsidies contingent upon export. Is it the US contention that, in order to be contingent on export, exportation must be the exclusive condition for receipt of the payment?

(99) How does the United States respond to Brazil's arguments in paragraphs 71-75 of Brazil's Oral Statement at the first session of the first panel meeting concerning the relevance of the Appellate body Report in US- FSC(21.5)

Brazil's Comment on US Answers:

125. The United States in its 11 August Answer to Question 93 states at paragraph 202 that “all upland cotton produced in the United States is eligible for the benefit of the Step 2 cotton subsidy”.¹¹⁴ Furthermore, it submits that “when the entirety of production of a good in a country is eligible to receive a subsidy, no contingency on export exists”.¹¹⁵

126. Brazil provides a detailed comment to these assertions in its Rebuttal Submission.¹¹⁶ In fact, Step 2 payments are not made to every pound of upland cotton that is “used”. Rather, Step 2 payments are made on every pound of upland cotton that is *exported by eligible exporters* or that is

¹¹⁰ Exhibit Bra-37 (7 CFR 1427.104)

¹¹¹ Exhibit Bra-37 (7 CFR 1427.108(d)).

¹¹² Exhibit US-21 (Upland Cotton Domestic User / Exporter Agreement, Section, Section B1)

¹¹³ Exhibit Bra-37 (7 CFR 1427.108(d))

¹¹⁴ US 11 August Answer to Question 93, para. 202.

¹¹⁵ US 11 August Answer to Question 93, para. 202.

¹¹⁶ See Rebuttal Submission of Brazil, paras. 129-130.

used by eligible domestic users. No Step 2 payment is made for upland cotton exported or used by ineligible persons, or for upland cotton that is neither used domestically nor exported, but that is for instance stored, stolen or incidentally destroyed by for example fire.

127. Furthermore, the criterion whether Step 2 payments are available to all upland cotton produced in the United States is entirely irrelevant for Brazil's claims under Article 3 of the SCM Agreement. That provision prohibits the payment of subsidies that are contingent upon export or contingent upon the use of domestic over imported goods. It follows that a subsidy is prohibited if its payment is conditional on the existence of one of the two situations: export or use of local content.

(107) At paragraph 135 of its first written submission, the United States states: "The subsidy is not contingent upon export performance..."(emphasis added). Again, in the course of the first Panel meeting, the United States admitted that the Step 2 payments were "subsidies". Does the United States thus concede that Step2 payments constitute a "subsidy" within the meaning of the WTO Agreement?

Brazil's Comment on US Answer:

128. The arguments provided by the United States are not responsive to the question posed by the Panel. Brazil reiterates that Exhibit Bra-69 is not relevant for its *de jure* claims. Whenever a Step 2 payment for exported or domestically used upland cotton takes place, the payment is made inconsistently with Articles 3.1(a) or 3.1(b) of the SCM Agreement and with Articles 3.3 and 8 of the Agreement on Agriculture in the case of Step 2 export payments. Step 2 export payments are contingent upon export performance and Step 2 domestic payments are contingent upon use of domestic over imported upland cotton. Neither the respective share of Step 2 export and domestic payments nor the share of eligible US upland cotton production materially affects this conclusion.

(111) Does the United States maintain its argument that actions based on Article 3.1(b) of the SCM Agreement are conditionally « exempt from actions » due to the operation of Article 13 of the Agreement on Agriculture?

(112) In the event that the Panel finds that Article 6.3 of the Agreement on Agriculture does not preclude an examination of Brazil's claims under Article 3.1 of the SCM Agreement and Article III:4 of GATT 1994, how does the United States respond to the merits of Brazil's claims relating to Step 2 payments under those provisions?

(113) Is it necessary for measures directed at agricultural processors included in AMS to discriminate on the basis of the origin of goods?

(115) What is the meaning and relevance (if any) to Brazil's claims under Article 3 of the SCM Agreement and Article III:4 of GATT 1994 of the phrase "measures directed at agricultural processors shall be included to the extent that such measures benefit the producers of the basic agricultural products" in the Agreement on Agriculture?

(116) With respect to paragraph 32 of the oral statement of the EC, are subsidies contingent on the use of domestic goods consistent with the Agreement on Agriculture? Does the phrase "provide support in favour of domestic producers" in Article 3.2 of the Agreement on Agriculture refer to, and/or permit such subsidies?

Brazil's Comment to the US Answers:

129. Brazil addresses the US 11 August Answers to the questions listed above in its Rebuttal Submission at paragraphs 131-144. Brazil further refers the Panel to paragraphs 78-86 of its Oral Statement and to its 11 August Answers to Questions 100-102 and 115-116.

ANNEX I-4

Please refer to Section V. of Annex D-4.

ANNEX I-5

ANSWERS OF BRAZIL TO QUESTIONS POSED BY THE PANEL FOLLOWING THE RESUMED FIRST SUBSTANTIVE MEETING OF THE PANEL

27 October 2003

TABLE OF CONTENTS

	<u>Page</u>
A. REQUEST FOR PRELIMINARY RULINGS.....	174
B. EXEMPTION FROM ACTIONS.....	175
C. IDENTIFICATION OF THE SUBSIDIZED PRODUCT.....	175
F. PROHIBITED SUBSIDIES.....	188
G. SPECIFICITY/CROP INSURANCE.....	190
H. EXPORT CREDIT GUARANTEES.....	195
I. ACTIONABLE SUBSIDIES	203
J. CAUSATION.....	213
K. ARTICLE XVI OF GATT 1994.....	226
L. CLARIFICATIONS.....	234

Table of Cases

Short Title	Full Case and Citation
<i>EC – Sugar Exports II (Brazil)</i>	GATT Panel Report, <i>European Communities – Refunds on Exports of Sugar Complaint by Brazil</i> , L/5011 – 27S/69, adopted 10 November, 1980.
<i>EEC – Wheat Flour</i>	GATT Panel Report, <i>European Economic Community – Subsidies on Export of Wheat Flour</i> , SCM/42, circulated 21 March 1983.
<i>EC - Hormones</i>	Appellate Body Report, <i>EC Measures Concerning Meat and Meat Products (Hormones)</i> , WT/DS26/AB/R, adopted 13 February 1998.
<i>EC- Bananas</i>	Appellate Body Report, <i>European Communities – Regime for the Importation, Sale and Distribution of Bananas</i> , WT/DS27/AB/R, adopted 25 September 1997.
<i>Argentina – Textiles and Apparel</i>	Panel Report, <i>Argentina – Measures affecting Imports of Footwear, Textiles, Apparel and Other Items</i> , WT/DS56/R, adopted 22 April 1998.
<i>Canada - Aircraft</i>	Appellate Body Report, <i>Canada – Measures Affecting the Export of Civilian Aircraft</i> , WT/DS70/AB/R, adopted 20 August 1999.
<i>India – Quantitative Restrictions</i>	Panel Report, <i>India – Quantitative Restrictions on Imports of Agricultural, Textile and Industrial Products</i> , WT/DS90/R, adopted 22 September 1999.
<i>Korea – Dairy Safeguards</i>	Appellate Body Report, <i>Korea – Definitive Safeguard Measure on Imports of Certain Dairy Products</i> , WT/DS98/AB/R, adopted 12 January 2000.
<i>US - FSC</i>	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporation”</i> , WT/DS108/AB/R, adopted 20 March 2000.
<i>US – FSC (21.5)</i>	Appellate Body Report, <i>United States – Tax Treatment for “Foreign Sales Corporation.”</i> Recourse to Article 21.5 of the DSU by the European Communities. WT/DS108/AB/R, adopted 29 January 2002.
<i>Argentina – Footwear Safeguards</i>	Appellate Body Report, <i>Argentina – Safeguard Measures on Imports of Footwear</i> , WT/DS121/AB/R, adopted 12 January 2000.
<i>US – Section 301</i>	Panel Report, <i>United States – Sections 301-310 of the Trade Act of 1974</i> , WT/DS152/R, adopted 27 January 2000.
<i>EC - Sardines</i>	Appellate Body Report, <i>European Communities – Trade Descriptions of Sardines</i> , WT/DS231/AB/R, adopted 23 October 2002.

List of Exhibits

“Production and Trade Policies Affecting the Cotton Industry,” ICAC, September 2003	Exhibit Bra- 284
“Agriculture Fact Book 2001-2002,” Chapter 3 – American Farms.	Exhibit Bra- 285
Direct and Counter-Cyclical Programme Contract, Form CCC-509, USDA, Commodity Credit Corporation	Exhibit Bra- 286
Market Revenue and US Government Payments to US Upland Cotton Producers.	Exhibit Bra- 287
“NASS to Update Acreage If Necessary,” National Agricultural Statistics Service, USDA, 29 September 2003.	Exhibit Bra- 288
7 CFR 1412.606; 7 CFR 718.102, 2003 Edition	Exhibit Bra- 289
“Farmers Must File Acreage to Receive 2002 Payments,” Kansan Online Ag Briefs; AFBIS Inc. Crop Watch, June 2003	Exhibit Bra- 290
“Direct and Counter-Cyclical Payment Programme”, Farm Service Agency, USDA, April 2003.	Exhibit Bra- 291
7 CFR 718.102, 2002 Edition	Exhibit Bra- 292
Data for Acreage Chart	Exhibit Bra- 293
“The World Fact Book – Benin,” CIA.	Exhibit Bra- 294
2004 US Budget, Federal Credit Supplement, Introduction and Table 2	Exhibit Bra- 295
“USDA Announces \$2.8 Billion in Export Credit Guarantees,” FAS Press Release, 30 September 2003	Exhibit Bra- 296
7 U.S.C § 5641(b)(1); 7 U.S.C. § 5622(a), (b)	Exhibit Bra- 297
“USDA Amends Commodity Eligibility under Credit Guarantee Programmes”, FAS Press Release, 24 September 2002.	Exhibit Bra- 298
“Summary of FY 2003 Export Credit Guarantee Programme Activity”, USDA, Covering GSM-102, GSM 103 and SCGP	Exhibit Bra- 299
Calculation on US Rice Exports Benefiting from GSM-102, GSM-103 and SCGP.	Exhibit Bra- 300
Additional Results from Professor Sumner’s Model.	Exhibit Bra- 301
Revised and Extended Data on Article 6.3(d) Claim.	Exhibit Bra- 302

John C. Beghin and Holger Matthey. “Modelling World Peanut Product Markets: A Tool for Agricultural Trade Policy Analysis”. Center for Agricultural and Rural Development (CARD), May 2003.	Exhibit Bra- 303
John C. Beghin, Barbara El Osta, Jay R. Cherlow, and Samarendu Mohanty. “The Cost of the US Sugar Programme Revisited”, Centre for Agricultural and Rural Development (CARD), March 2001.	Exhibit Bra- 304
Larry Salathe, J. Michael Price and David Banker. “An Analysis of the Farmer Owned Reserve Programme 1977-82. American Journal of Agricultural Economics, February 1984.	Exhibit Bra- 305
“Supply Response under the 1996 Farm Act and Implications for the US Field Crops Sector,” Lin et al., USDA, July 2000.	Exhibit Bra- 306
Change in US and World Exports in Per cent.	Exhibit Bra- 307
“Decoupled Payments: Household Income Transfers in Contemporary US Agriculture,” ERS, Agriculture Economic Report N° 822.	Exhibit Bra- 308
Barnard C., Nehring, R., Ryan, J., Collender, R. “Higher Cropland Values from Farm Programme Payments: Who Gains?” Economic Research Service. USDA, Agricultural Outlook November 2001.	Exhibit Bra- 309
“The Incidence of Government Payments on Agricultural Land Rents: The Challenges of Identification,” Roberts, Kirwan and Hopkins, August 2003, American Journal of Agricultural Economics.	Exhibit Bra- 310
Side by Side Chart of the Weekly US Adjusted World Price, the A Index, the nearby New York Futures Price, the Average US Spot Market Price and Prices Received by US Producers from January 1996 to the present.	Exhibit Bra- 311
Cotton Outlook Reports dated 7 June 2002, 27 September 2002 and 4 October 2002.	Exhibit Bra- 312

A. REQUEST FOR PRELIMINARY RULINGS

122. Does Brazil allege that cottonseed payments, interest subsidies and storage payments are included in the subsidies that cause serious prejudice? Do they appear in the economic calculations? BRA

Brazil's Answer:

1. Cottonseed payments, interest subsidies and storage payments are included in the set of subsidies that Brazil alleges cause serious prejudice to its interests within the meaning of Articles 5(c) and 6.3 of the SCM Agreement and Article XVI of GATT 1994. The amounts of cottonseed payments and interest subsidies/storage payments range from \$50 million to \$216 million per year.¹ To appreciate the size of these subsidies, the annual amount of each of them separately far exceeds the total amount of Brazilian assistance to its upland cotton farmers of \$10 million in MY 2001 by a factor of 4 to 21.² Indeed, the annual, individual amount of US cottonseed payments, interest subsidies and storage payments also by far exceeds the amounts of subsidies paid by most other cotton-producing countries.

2. The United States has notified cottonseed payments as trade-distorting amber box subsidies to the WTO.³ Thus, these payments are presumed to be trade-distortive. Interest subsidies and storage payments appear to be part of the operation of the marketing loan programme that has also been notified to the WTO as a trade-distortive amber box subsidy, and is therefore presumed to be trade-distortive. The United States has not notified them separately to the WTO.⁴

3. The economic calculations provided by Brazil on the effect of US subsidies in filling the cost revenue gap include cottonseed payments and interest subsidies/storage payments.⁵ They are also included as part of the overall level of US subsidization provided. However, they are not part of the econometric model developed by Professor Daniel Sumner.⁶

123. Does Brazil's request for the establishment of the Panel name the statute authorizing cottonseed payments for the 1999 crop? BRA

Brazil's Answer:

4. To the extent that cottonseed payments for the MY 1999 crop were authorized by Section 204(e) of the Agricultural Risk Protection Act of 2000, Brazil's request for the establishment of the Panel names the statute authorizing these payments.⁷ This act authorized the payment of \$100 million in cottonseed payments. However, Brazil did not explicitly identify in its request for establishment P.L. 106-113, which serves as the legal basis for a further \$79 million in cottonseed payments for the MY 1999 cottonseed payments.

¹ Brazil's 9 September Further Submission, Table 1, p. 4.

² Exhibit Bra-284 ("Production and Trade Policies Affecting the Cotton Industry," ICAC, September 2003, p. 6).

³ Exhibit Bra-47 (G/AG/N/USA/43, p. 20).

⁴ Exhibit Bra-47 (G/AG/N/USA/43, p. 20).

⁵ Brazil's 22 August Rebuttal Submission, para. 30 and 40.

⁶ To the extent that interest subsidies and storage payments operate to compensate for any cost incurred by US upland cotton producers from the participation in the marketing loan program (for instance, for the storage cost resulting from storing physical upland cotton as collateral for the marketing loan), these subsidies have been considered in Professor Sumner's model. However, those costs do not occur, if a producer decides to opt for a loan deficiency payment rather than taking out a marketing loan.

⁷ WT/DS267/7, p. 2.

5. Brazil emphasizes that it is not challenging the underlying statutes authorizing the payment of cottonseed payments in MY 1999, 2000 and 2002, *i.e.*, Brazil does not challenge those payments *per se*. Brazil challenges as “measures” the payments of those subsidies as causing adverse effects to its interests. The United States and Brazil have consulted about those payments.⁸ Brazil properly included reference to all “payments” for upland cotton in its request for the establishment of the Panel.⁹ This is sufficient to properly identify cottonseed payments as measures for the purposes of Brazil’s request for the establishment of the Panel.

B. EXEMPTION FROM ACTIONS

6. **According to its revised timetable, the Panel will issue its report to the parties after the end of the 2003 calendar year. Does this have any impact on “exempt[ion] from actions” under Article 13(b)(ii) and 13(c)(ii) of the *Agreement on Agriculture*? BRA, US**

Brazil’s Answer:

6. No. Brazil’s claims relate to prohibited and actionable subsidies provided during MY 1999-2002 when the United States had no peace clause protection. Brazil’s threat of serious prejudice claims relate to the present threat of serious prejudice caused by subsidies provided during MY 1999-2002, as well as the threat caused by subsidies that are required to be provided through the end of MY 2007 by the 2002 FSRI Act and the 2000 ARP Act. The fact that the Panel will issue its determination regarding these subsidies after the termination of the “peace clause” in 2004 has no impact on the analysis of these claims.

C. IDENTIFICATION OF THE SUBSIDIZED PRODUCT

125.

(2) **Brazil has submitted that "The record suggests that *historic* producers are *current* producers." It points to factors including the specialization of upland cotton producers, the need to recoup expensive investments in cotton-specific equipment, and the geographic focus and climatic requirements of upland cotton production in the "cotton belt". (Brazil's rebuttal submission, footnote 98, on page 24)**

(a) **Regarding the specialization of upland cotton producers and the geographic focus of upland cotton production, how does Brazil take account of the fact that cotton is produced in 17 of the 50 states of the United States and that average cotton area is approximately 38% of a cotton farm's acres? (This information is taken from the US's response to question 67*bis*, footnote 35). BRA**

⁸ Exhibit Bra -101 (Questions for the Purposes of the Consultations, Questions 14.1 *et seq.*, p. 13).

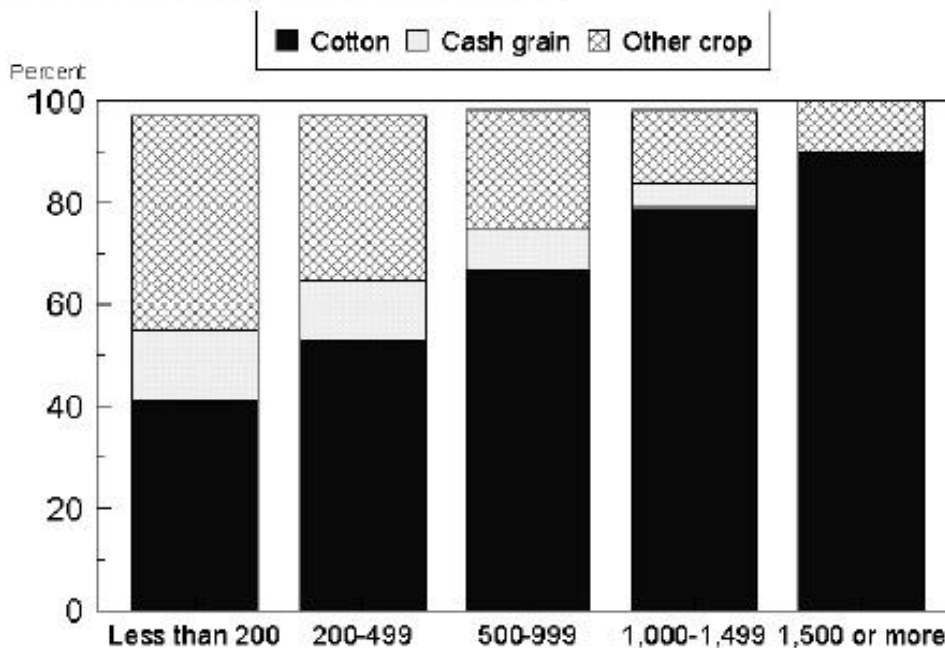
⁹ The “measures” identified include (1) “domestic support subsidies provided to the US upland cotton industry during marketing years 1999-2001”, (2) “domestic support subsidies that are mandated to be provided to the US upland cotton industry during marketing years 2002-2007”, (3) “all subsidies benefiting upland cotton that have trade distorting effects or effects on production by the US upland cotton industry”, (4) “domestic support, and all other subsidies provided under regulations, administrative procedures . . . for the production, use and/or export of US upland cotton and upland cotton products”. WT/DS267/7, pages 1, 2, 3.

Brazil's Answer:

7. In contrast to the information cited in the Panel's question, more relevant information concerning specialization of cotton producers in cotton farms is set out in Exhibit Bra-16, which is a 2001 USDA report on the cost of production of cotton farms. That report contains the following figure:¹⁰

Figure 3 Specialization of cotton farms

Ninety percent of farms with 1,500 or more cotton acres specialized in cotton while roughly 40 percent of farms with less than 200 cotton acres specialized in either cotton or other crops.



Source: 1997 Agricultural Resource Management Study, cotton version

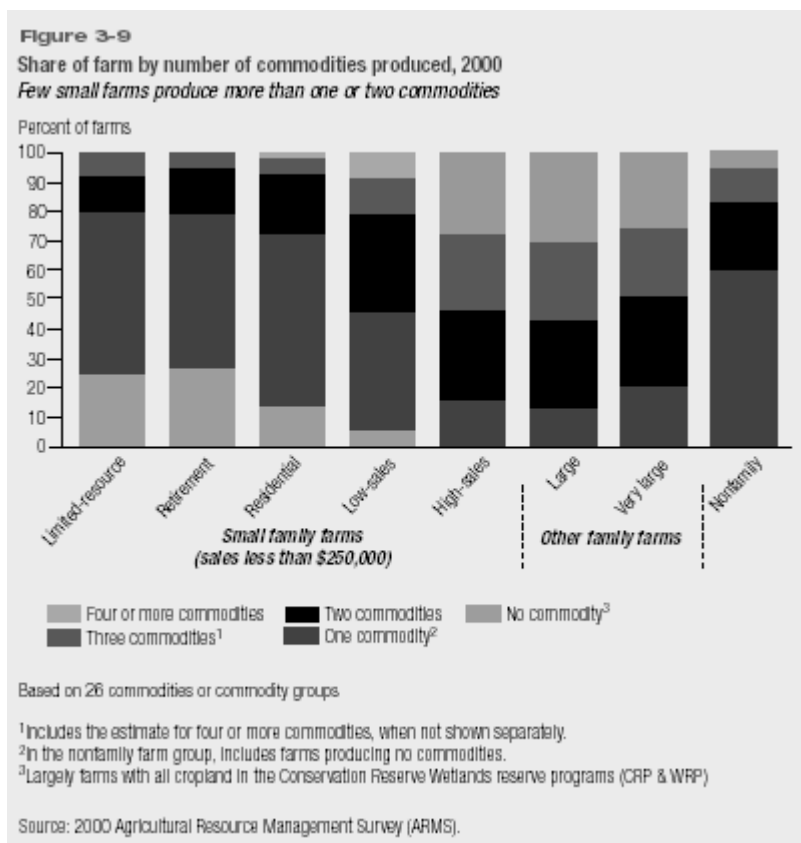
8. This evidence shows that farms with 500 or more acres of upland cotton are heavily specialized in the production of cotton. While these farms represented 33 per cent of US farms producing upland cotton, they produced 75 per cent of total US upland cotton in MY 1997.¹¹ Thus, the great majority of US production of upland cotton takes place on farms that largely specialize in the production of upland cotton.

9. Other data regarding specialization is found in a 1998 USDA report indicating that most smaller farms – defined as farms with income below \$250,000 and which account for 92 per cent of all US farms – tend to produce only one or at most two crops.¹² This is illustrated in the chart below:

¹⁰ Exhibit Bra-16 (“Characteristics and Production Costs of US Cotton Farms”, USDA, October 2001, p. 9).

¹¹ Exhibit Bra-16 (“Characteristics and Production Costs of US Cotton Farms”. USDA, October 2001, p. 7).

¹² Exhibit Bra-285 (“Agriculture Fact Book 2001-2002”, Chapter 3 - American Farms, p. 32).



10. Approximately 55 per cent of upland cotton is produced on such smaller farms.¹³ Thus, even for those smaller farms producing upland cotton, the evidence suggests that over 50 per cent produce mainly upland cotton and the rest produce at most one additional crop. This evidence is consistent with Brazil's argument concerning cotton specialization.

11. With respect to the Panel's question, the 38 per cent figure cited by the United States refers to "planted cotton acreage" as a percentage of "total acreage operated".¹⁴ The United States provides no information on what "total acreage operated" means. Nor does the United States provide the Panel with the amount of "planted cotton acreage" as a percentage of "total PFC/DP base acreage". It may be that the cotton acreage accounts for most of a farm's "base acreage". Thus, the "total acreage operated" is not the appropriate basis to calculate a percentage of base acreage for farms producing upland cotton. The best evidence of specialization is the actual payments made to upland cotton producers discussed in Brazil's Answer to Question 125 (5). The next best evidence is the USDA data on specialization of cotton farms cited above.

12. Moreover, Brazil's arguments are not dependent on proof that the majority of cotton farms produce *only* upland cotton. The evidence suggests that larger farms tend to grow at least some other crops and, therefore, may have more than one type of PFC/market loss assistance or direct and counter-cyclical payment "base acreage".¹⁵ As Christopher Ward testified, farmers rotate the production of several different crops, planting one crop on a certain portion of the farmland, and then

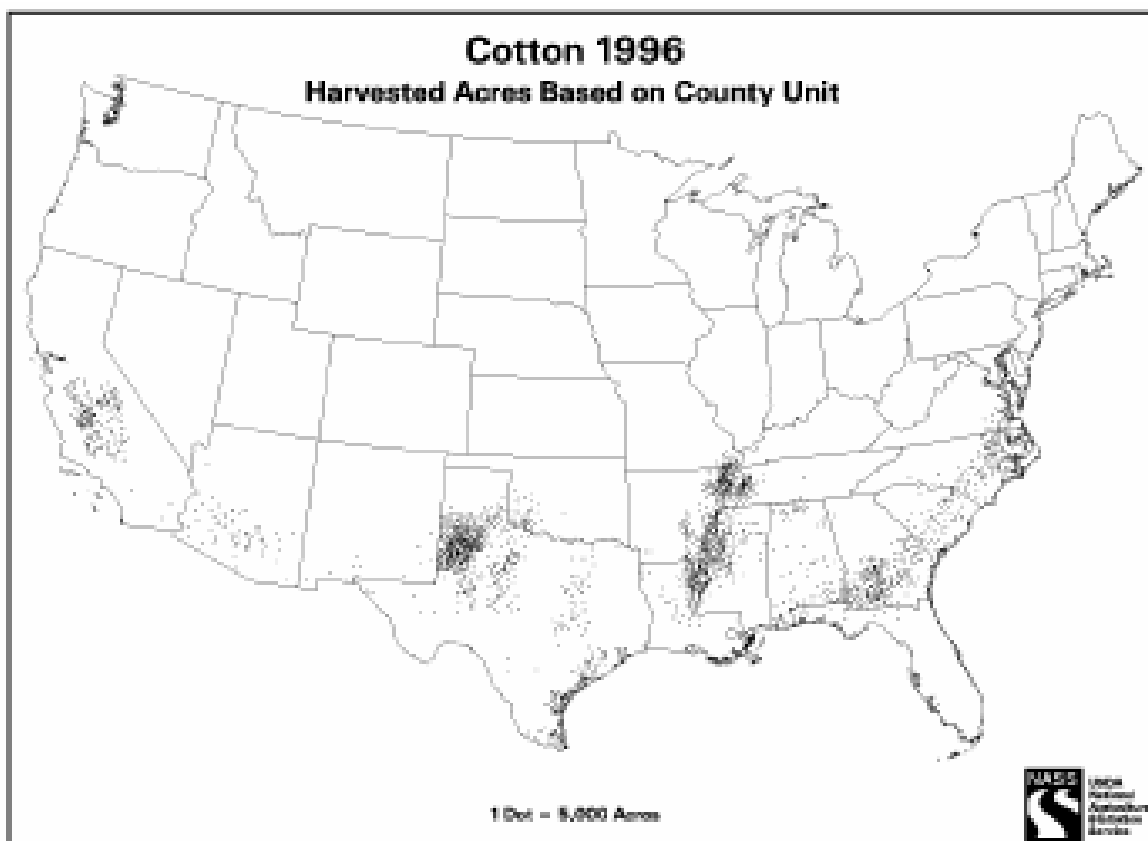
¹³ Exhibit Bra-16 ("Characteristics and Production Costs of US Cotton Farms," USDA, October 2001, Table 7) tabulating farms with value of production less than \$250,000.

¹⁴ Exhibit Bra-16 ("Characteristics and Production Costs of US Cotton Farms," USDA, October 2001, Table 3).

¹⁵ This is also demonstrated by Exhibit Bra-286 (Direct and Counter-cyclical Program Contract, Form CCC-509, USDA, Commodity Credit Corporation), which provides for the possibility to establish base acres for different crops.

moving the production of that same crop to another portion of the farmland.¹⁶ But the fact that crops are rotated or that some farmers have multiple types of “base acres” and produce more than one crop on their farm does not mean that farmers do not continue to plant upland cotton and use cotton-specific machinery and ginning facilities. This is confirmed by the fact that between MY 1999-2002, there were no wide swings in planted upland cotton acreage.¹⁷

13. Finally, while the United States is correct in stating that upland cotton is produced in 17 states, 66 per cent of upland cotton is produced in only 5 states, and 90 per cent is produced in only 10 out of the 50 US states.¹⁸ In addition, even within each of these 10 states, upland cotton tends to be grown in relatively distinct geographical regions. This is shown in the graph below:¹⁹



(c) **Regarding the high cost of upland cotton production, can Brazil show that farms who planted upland cotton could only have covered their costs by receiving upland cotton, rice or peanut payments in every year from 1999 through 2002? BRA**

Brazil's Answer:

14. Between MY 2000-2002, US upland cotton producers could not make a profit, unless they grew upland cotton on upland cotton or rice (or peanut in MY 2002) base acreage. Brazil provides data below for each of the four marketing years covering the period of investigation (MY 1999-2002). This evidence is consistent with a conclusion that the great majority of upland cotton was produced on upland cotton base acreage. In responding to this question from the Panel, Brazil took into account

¹⁶ Exhibit Bra-283 (Statement of Christopher Ward – 7 October 2003, para. 2)

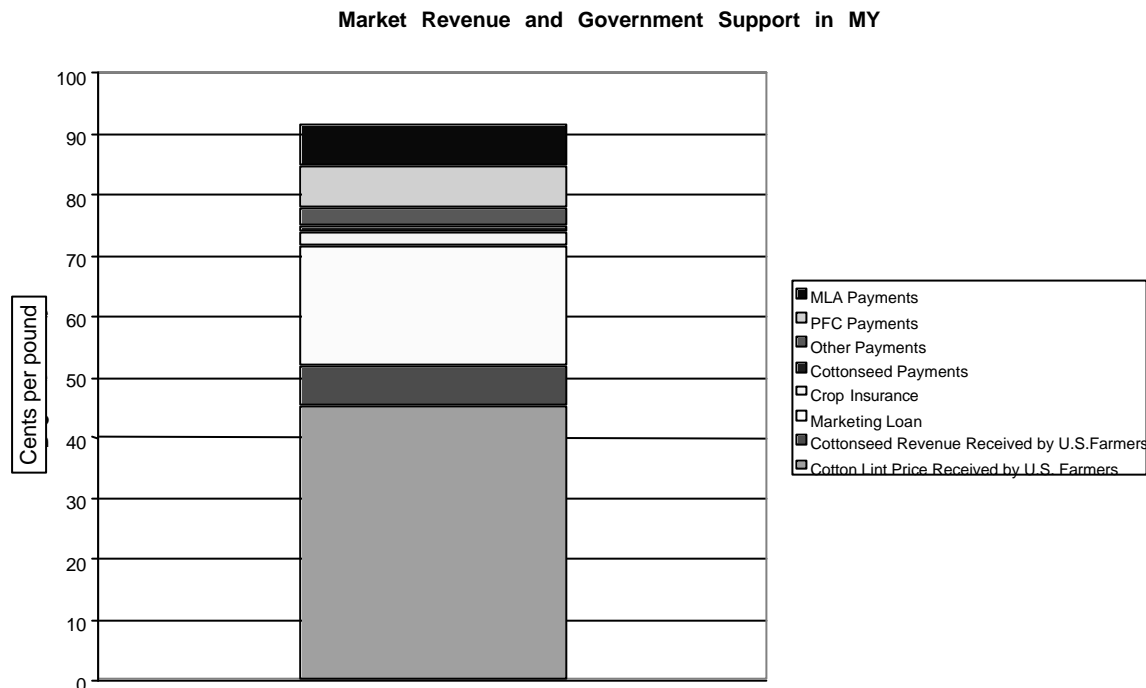
¹⁷ See Brazil's Answer to Question 125(6).

¹⁸ Exhibit Bra-107 (US and State Farm Income Data, Farm Cash Receipts, ERS, USDA, June 2003).

¹⁹ <http://usda.mannlib.cornell.edu/reports/nassr/field/planting/uph97.pdf> , Usual Planting and Harvesting Dates for US Field Crops, National Agricultural Statistics Service, USDA, December 1997, p. 7.

Dr. Glauber's comment that Step 2 payments are not received by US upland cotton producers but rather by exporters and domestic users.²⁰ Brazil generally agrees with this statement. Therefore, Brazil has excluded Step 2 payments from the pool of revenue received by US upland cotton producers.²¹ It presents data on the total amount of market revenue for upland cotton lint and seed, marketing loan benefits, crop insurance payments, cottonseed payments, so-called "other payments"²² and PFC, market loss assistance, direct and counter-cyclical payments.

15. The following chart shows revenues of upland cotton producers in MY 1999:²³



16. The chart shows that US upland cotton producers received total revenue of 91.54 cents per pound of upland cotton produced. At the same time, the average cost of production was 82.03 cents per pound in MY 1999²⁴ and prices received by producers were 45 cents per pound.²⁵ It follows that US producers could not produce upland cotton without the financial assistance of the US Government in the form of large amounts of subsidies. US producers needed 4.46 cents per pound from the total combined upland cotton PFC and market loss assistance payment of 13.97 cents per pound to recover their costs.²⁶

²⁰ Exhibit US-24, p. 3 fifth and sixth paragraph.

²¹ This does not affect Brazil's view that Step 2 payments are properly included in the peace clause analysis under Article 13(b)(ii) of the Agreement on Agriculture as "support to upland cotton". While Step 2 payments may not directly benefit domestic producers of upland cotton, they do so indirectly. As they increase demand for US upland cotton, they increase prices received by US producers and are, therefore, properly described as "support to upland cotton".

²² Interest subsidies and storage payments.

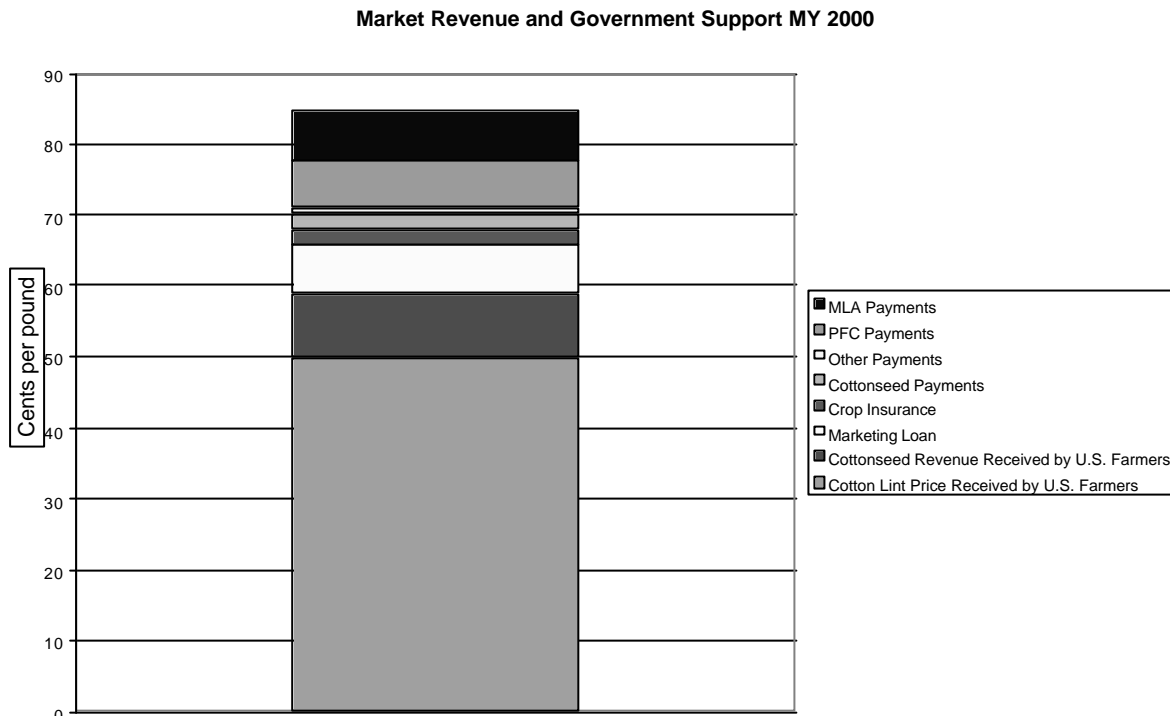
²³ See Exhibit Bra-287 (Market Revenue and US Government Payment to US Upland Cotton Producers).

²⁴ Exhibit Bra-205 (Costs and Revenues of US Upland Cotton Producers).

²⁵ Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 5).

²⁶ Thus, they could have produced upland cotton on wheat, corn, grain sorghum, cotton and rice base acreage without suffering a loss.

17. In MY 2000, the financial situation of US upland cotton producers worsened. While the price they received for upland cotton lint increased to 49.8 cents per pound²⁷, their total revenue fell to 84.74 cents per pound²⁸, only slightly above their average cost of production of 82.69 cents per pound.



18. Again, large amounts of US subsidies were instrumental in closing the gap between the US cost of production and the market returns of producers. For MY 2000, the 13.86 cents per pound in upland cotton PFC and market loss assistance payments as well as all other subsidies were needed to close the gap between the cost of production and the market returns.²⁹ Average US upland cotton producers could also have covered their total costs had they planted upland cotton on rice base acres. But they would have suffered a marginal loss on corn or other crop base acres.

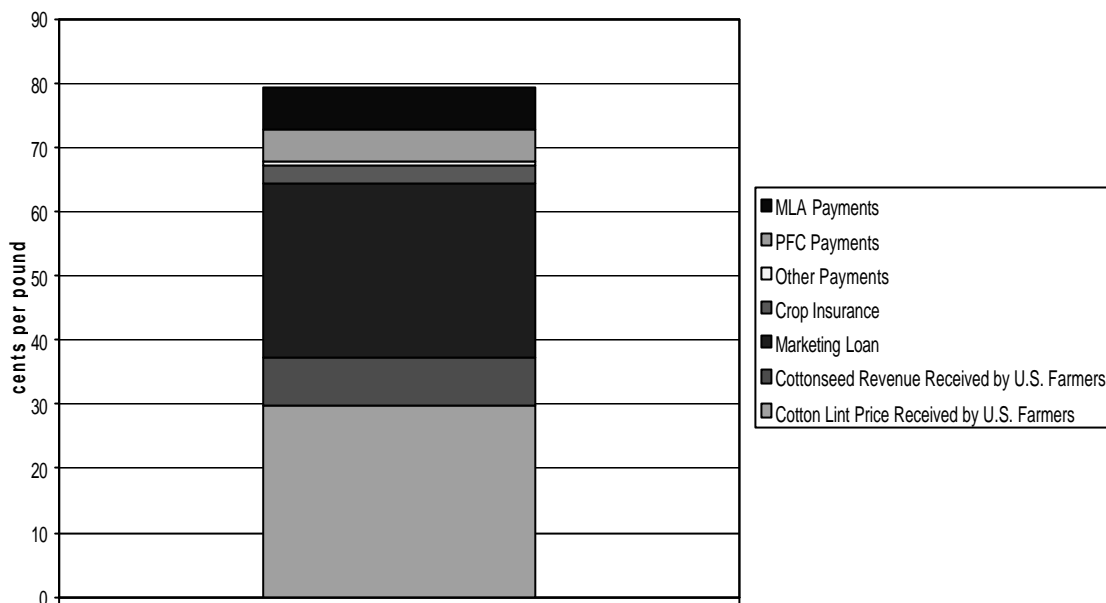
19. The results for MY 2001 show a similar result:

²⁷ Exhibit Bra-4 (“Fact Sheet: Upland Cotton”, USDA, January 2003, p. 5).

²⁸ See Exhibit Bra-287 (Market Revenue and US Government Payment to US Upland Cotton Producers).

²⁹ See Exhibit Bra-287 (Market Revenue and US Government Payment to US Upland Cotton Producers).

Market Revenue and Government Support in MY 2001



20. US producers received a total revenue of 79.41 cents per pound,³⁰ only 29.8 cents per pound of which was market revenue for upland cotton lint. At the same time, they faced an average cost of production of 76.44 cents per pound.³¹ Thus, the average US producer of upland cotton needed an upland cotton or rice PFC and market loss assistance payment to break even, while upland cotton production on corn or any other crop base acreage would have generated a loss.

21. For MY 2002, average US producers even suffered a loss from upland cotton production on upland cotton base acres³², let alone corn or other crop base acres, except for rice and peanuts.³³ The average US upland cotton producer received total revenues of 82.96 cents per pound³⁴, while their average total cost for MY 2002 was 83.59 cents per pound.³⁵

³⁰ See Exhibit Bra-287 (Market Revenue and US Government Payment to US Upland Cotton Producers).

³¹ Exhibit Bra-205 (Costs and Revenues of US Upland Cotton Producers).

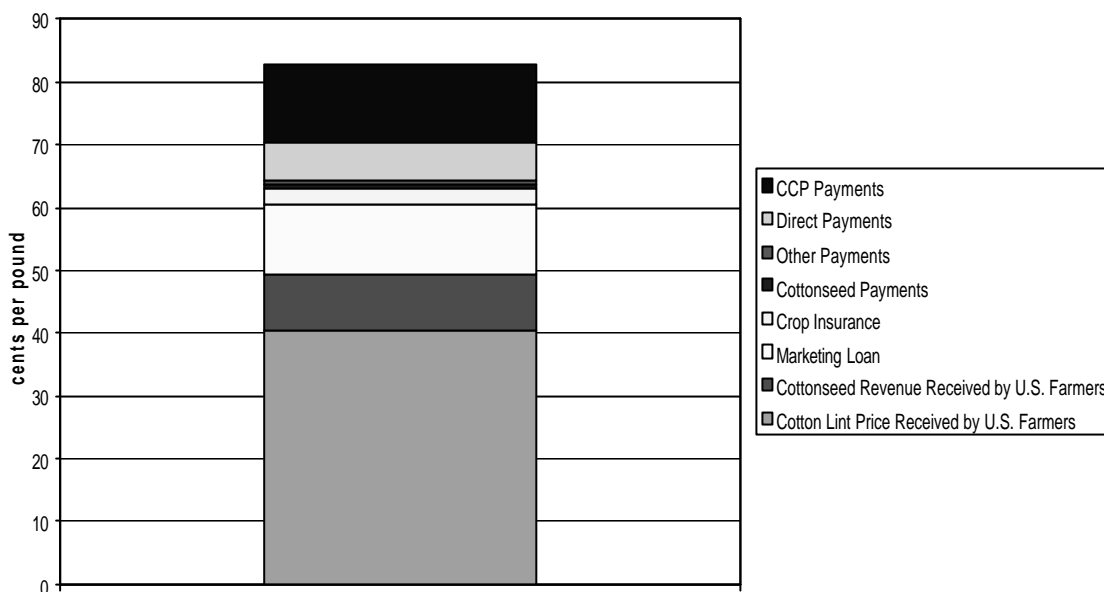
³² Brazil notes that it is not in a position to quantify the effect of the yield update for purposes of the counter-cyclical payments and, thus, likely underestimated the amount of those payments (See Brazil's Answer to Questions 125 (8)). With slightly higher counter-cyclical payments than assumed by Brazil, US producers of upland cotton might have made a small profit in MY 2002.

³³ Brazil notes that while evidently some former corn producers had shifted to upland cotton production, the fact that they were allowed to update their base acres to upland cotton base acres meant that they could now receive upland cotton payments (See Brazil's Answer to Question 125 (7)).

³⁴ See Exhibit Bra-287 (Market Revenue and US Government Payment to US Upland Cotton Producers).

³⁵ Exhibit Bra-205 (Costs and Revenues of US Upland Cotton Producers).

Market Revenue and Government Support in MY 2002



22. The overall conclusion of this analysis is that, on average over the period of investigation, US upland cotton producers needed and received upland cotton or rice programme payments to cover (or almost cover) their total cost of production. At the same time, as total revenue decreased relative to the cost of production, US upland cotton acreage increased between MY 1999-2001.³⁶ Because upland cotton producers with non-upland cotton or rice base acreage would have lost money (even with the subsidies), they would have been forced to switch out of upland cotton production. This means that the only producers that could remain were those with upland cotton or rice base. The fact that upland cotton acreage increased through MY 2001 suggests that only a small portion of upland cotton in the United States could have been grown on non-upland cotton base acres.

23. Similarly, in MY 2002, the option to update the base acreage (and yield for the CCP payment programme) allowed those producers that produced on non-upland cotton base acres in MY 1998-2001 to receive the considerably higher upland cotton payments under the 2002 FSRI Act. Because it is not economically sustainable to grow upland cotton on non-upland cotton (-rice or -peanut) base, the ability to update suggests that by MY 2002 nearly all US producers grew on upland cotton base.

24. Moreover, the data above indicates that even with subsidies, the average US producers did not earn any or, at most, a small profit during MY 1999-2002. As Christopher Ward testified, there is a strong need to generate profits to stay in the upland cotton business.³⁷ These profits pay for investments in new machinery and technologies, as well as for losses incurred in years with low prices. But even with large subsidies, US producers only met their costs. Without subsidies, they were not even able to meet their variable cost in MY 2001.

25. In sum, during most of the period of investigation, US producers of upland cotton needed the high upland cotton payments from the PFC, market loss assistance, direct and counter-cyclical payment programmes to generate sustainable returns (MY 1999), simply break even (MY 2000-

³⁶ Exhibit Bra-4 (“Fact Sheet: Upland Cotton,” USDA, January 2003, p. 4). See also Brazil’s Answer to Question 125 (6).

³⁷ Exhibit Bra-283 (Statement of Christopher Ward – 7 October 2003, para. 10).

2001), or almost meet their total costs (MY 2002). It is, therefore, reasonable to assume that the great majority of US upland cotton was grown on upland cotton base acres.

(3) In calculating the amount of PFC, MLA, direct and counter-cyclical payments that went on upland cotton, Brazil made an adjustment for the ratio of current acreage to base acreage (see its answer to question 67, footnotes 2, 3, 4 and 5). Is this an appropriate adjustment for the particular factors referred to above? Why or why not? BRA, US

Brazil's Answer:

26. Brazil refers the Panel to its answers to Question 125 (8), Question 125(2)(a), and to Question 125(2)(c) for Brazil's arguments why its methodology is reasonable to use in the absence of direct evidence collected and controlled exclusively by the United States concerning the amount of those payments to upland cotton producers.³⁸ In the absence of such direct evidence, Brazil has set forth³⁹ extensive circumstantial evidence that US producers of upland cotton received such payments.⁴⁰

(4) Dr. Glauber has alleged that there are statistical problems in comparing planted acres to programme acres because of abandonment of crops and also because planted acres are only survey estimates, not reported figures (See Exhibit US-24, the first full paragraph in P2). Would it be more appropriate to divide harvested acreage by base acreage? What margin of error is there between the survey estimates and reported figures? BRA, US

Brazil's Answer:

27. The appropriate figures to use for farmers' decisions on upland cotton acreage are the official USDA figures for acres planted to upland cotton. Dr. Glauber discussed certain programme and statistical issues that may have applied in the early 1990s, but which – with the termination of the deficiency payment programme from MY 1996 on – are no longer relevant.⁴¹

28. The planted acre figures used by Brazil are the only official USDA data for planted acres of crops. These data are reported by the Farm Service Agency (FSA) in its Fact Sheet on Upland Cotton.⁴² Planted acres reflect the choice by farmers to commit land to upland cotton production by cultivating, fertilizing, seeding and applying other inputs during the pre-planting and planting period. In some parts of the United States, variable weather and other conditions mean that some land that has been planted to upland cotton, or to some other crops, is not harvested. But, there is no question that this land was committed at the time of planting to upland cotton production. Further, once the planting takes place, that decision generally precludes further upland cotton production (or other crops) for that marketing year.

29. According to USDA's National Agricultural Statistics Service (NASS), the procedure for measuring and reporting planted acres for upland cotton and other crops starts with a June survey of planted acres for each crop, which is well after planting commitments for upland cotton have been made early in spring. The June planted acre figures are updated in NASS files each month as additional data becomes available. Revisions in the figures on planted acres are determined in December and reported in the Crop Production report each year. These data include revisions based

³⁸ See also Brazil's 9 October Closing Statement, para. 2.

³⁹ Inferences drawn from this evidence satisfy Brazil's burden of proof in the absence of direct evidence. See Panel Report, *Argentina – Textiles and Apparel*, WT/DS56/R, para. 6.39.

⁴⁰ See Brazil's 9 October Closing Statement, Annex I for a summary of the evidence and further references.

⁴¹ Brazil notes that Dr. Glauber's assertions were made in the context of the acreage reduction and set aside requirements under the US deficiency payment programme.

⁴² Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4).

on FSA's certified acreage information. As Exhibit Bra-288 makes clear, NASS reported the 2003 revisions using FSA information in the October Crop Production report, rather than waiting until December.⁴³

(5) Do the acreage reports under section 1105(c) of the FSRI Act of 2002 indicate or assist in determining the number or proportion of acres of upland cotton planted on upland cotton base acres? Was there an acreage reporting requirement for upland cotton during MY1996 through 2002? BRA, US

Brazil's Answer:

30. The short answer to both of the Panel's questions is "yes". Regrettably, the United States has refused to provide Brazil or the Panel with the number or proportion of acres of upland cotton planted on upland cotton base acres for MY 1999-2002, despite Brazil's repeated efforts to obtain this information over the past year and despite the Panel's Question 67bis, in which the United States claimed incorrectly that it did not have access to this information.⁴⁴

31. As implemented, Section 1105(c) of the 2002 FSRI Act requires any recipient of direct and counter-cyclical payments to submit, as a condition of eligibility of receiving the payments, "annual acreage reports with respect to all cropland on the farm".⁴⁵ This means that the precise acreage for each crop grown on the farm must be tabulated and identified in an annual report. Depending on the state and the county, these acreage reports are generally due by the middle of each calendar year.⁴⁶

32. In addition to the annual acreage reports, the 2002 FSRI Act required all farms eligible for direct and counter-cyclical payments to file application forms establishing and proving their historic production of the 10 programme crops.⁴⁷ The required information includes the types, amount, and yields of all direct and counter-cyclical payment base acreages during the period 1998-2001 or reference to the earlier PFC base acreage. All of these applications were due no later than 1 June each year.⁴⁸ USDA reported in July 2003 that 99.6 per cent of eligible farms had completed the required applications and signed up for the direct and counter-cyclical programme.⁴⁹ Farms submitting both the annual programme acreage reports and the historic base-acreage application form were required to provide a specific farm identification number. This farm "ID" would appear to permit USDA to determine for each reporting farm the annual *acreage* mix of crops and the amount of direct and counter-cyclical base acreage for each one of those crops.

33. With respect to the period 1996-2001, the regulations under the 1996 FAIR Act required any recipient of PFC payments and marketing loans (or loan deficiency payment) to submit annual acreage reports for each of the commodities planted for harvest on a farm enrolled in such a programme.⁵⁰ This reporting requirement was a mandatory condition to receive payment. It would

⁴³ Exhibit Bra-288 ("NASS To Update Acreage If Necessary," National Agricultural Statistics Service, USDA, 29 September 2003).

⁴⁴ See US 27 August Comments on Brazil's Rebuttal Submission and Answer to Question 67bis, para. 21 (The United States admitted that it "tracked total expenditures," but denied that it collected or could derive the information requested by the Panel).

⁴⁵ Exhibit Bra-29 (Section 1105 of the 2002 FSRI Act) and Exhibit Bra-289 (7 CFR 1412.606) and Exhibit Bra-289 (7 CFR 718.102, 2003 edition).

⁴⁶ Exhibit Bra-290 ("Farmers must file acreage to receive 2002 payments," Kansan Online Ag Briefs, second paragraph); Exhibit Bra-290 (AFBIS Inc. Crop Watch, June 2003).

⁴⁷ Exhibit Bra-286 (Direct and Counter-cyclical Program Contract, Form CCC-509, USDA, Commodity Credit Corporation)

⁴⁸ Exhibit Bra-291 ("Direct and Counter-Cyclical Payment Program," Farm Service Agency, USDA, April 2003).

⁴⁹ Annex 2 to Exhibit Bra-105 (National Enrollment Report, USDA, 17 July 2003, last attachment).

⁵⁰ Exhibit Bra-292 (7 CFR 718.102, 2002 edition)

appear that the United States has collected precise acreage and payment information on (1) farms with PFC cotton base acreage, and (2) farms that produced upland cotton and received PFC and marketing loan payments. Combined with the specific farm identification number, this information would clearly permit the matching of information on a farm's crop base acreage and current planting and, thus, the collection of the amount and type of PFC (and market loss assistance) payments made to producers of upland cotton between MY 1999-2001.

34. In sum, the United States has exclusive control of the information that would provide the *amount* and *type* of PFC, market loss assistance, direct and counter-cyclical payments made by the US Government to US cotton producers during MY 1999-2002. The United States also has not provided information regarding the amount of updated upland cotton direct and counter-cyclical payment base acreage, the average yields applying to that (updated) base acreage, or the total amount of direct and counter-cyclical payment funds paid to holders of upland base acreage for MY 2002. All of this information is exclusively in the control of the United States and was first requested by Brazil over a year ago.⁵¹ The Panel first requested this information in August 2003.⁵² If the United States continues to refuse to provide this information, then Brazil submits that the Panel must either (1) draw adverse inferences that the information retained by the United States reflects greater payments than those estimated by Brazil,⁵³ or alternatively, (2) rely on Brazil's estimate that the payments equal total upland cotton base acreage payments times the ratio of upland cotton planted acreage to upland cotton base acreage.

(6) Please prepare a chart showing upland cotton base acreage, planted acreage and harvested acreage for MY1996 through 2002. Does the planted acreage fluctuate within a broad band? If not, does this indicate any stability in decisions to plant the same acres to upland cotton? BRA, US

Brazil's Answer:

35. Brazil has prepared the requested chart showing the developments of upland cotton base acreage, planted acreage and harvested acreage between MY 1996-2002.⁵⁴ The chart below shows that planted acreage does *not* fluctuate within a *broad* band. Instead, planted acreage fluctuates between a low of 13.1 million acres in MY 1998 and a high of 15.5 million acres in MY 2001.⁵⁵

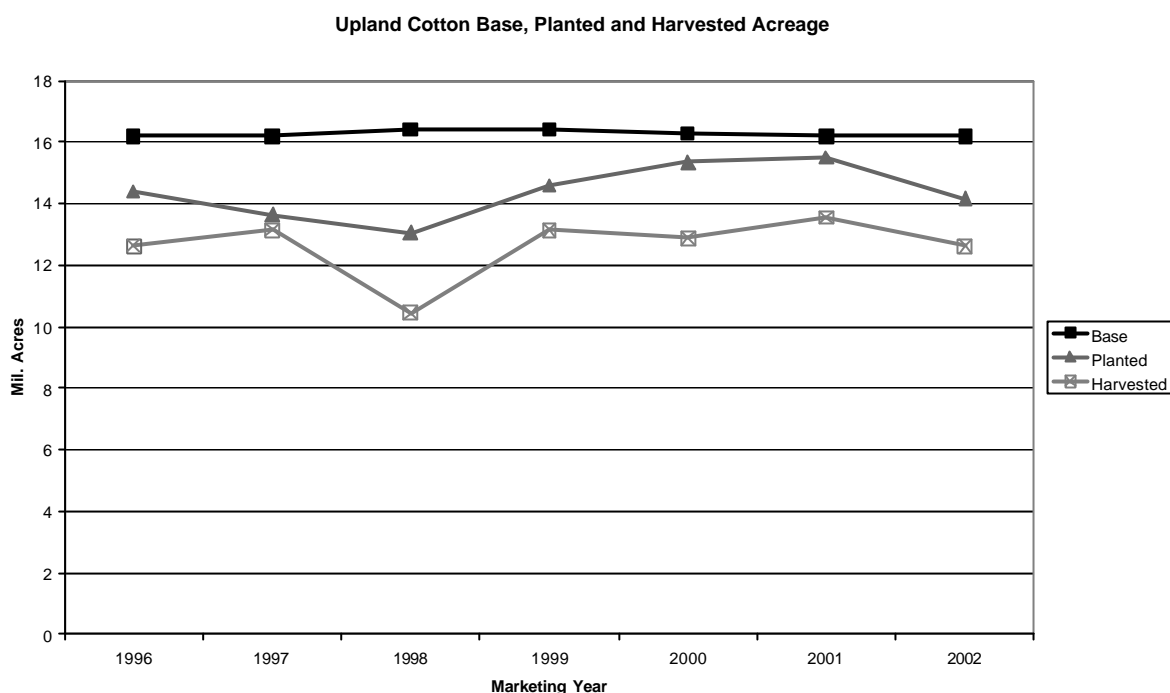
⁵¹ Exhibit Bra-49 (Brazil's Questions for the Purposes of Annex V Procedure, March 2003) and Exhibit Bra-101 (Brazil's Questions for the Purposes of the Consultations, 22 November 2002)

⁵² Question 67bis.

⁵³ The Appellate Body in *Canada – Aircraft* addressed the issue of drawing adverse inferences from a party's refusal to provide information requested by a panel. It stated that "a panel has the legal authority and the discretion to draw inferences from the facts before it." Moreover, it stated that a panel should examine very closely whether the full *ensemble* of the facts on the record reasonably permits the inference urged by one of the parties to be drawn, because a party's refusal to collaborate has the potential to undermine the functioning of the dispute settlement system. Furthermore, the Appellate Body noted that if it had been "deciding the issue that confronted the Panel, we might well have concluded that the facts of record did warrant the inference that the information Canada withheld . . . included information prejudicial to Canada's denial that the EDC had conferred a benefit and granted a prohibited export subsidy." (Appellate Body Report, *Canada – Aircraft*, WT/DS70/AB/R, para. 205).

⁵⁴ Brazil again notes that it is not in a position to provide the updated MY 2002 base acreage, but uses the upland cotton PFC base acreage for that year.

⁵⁵ Exhibit Bra-293 (Data for Acreage Chart).



36. Indeed, aggregate producers' decisions to plant upland cotton are fairly stable. Despite drastic changes in upland cotton prices, the amount of planted acres only varies within a narrow range, confirming that US producers are largely isolated from upland cotton market price incentives. The data shown in this chart is also consistent with Brazil's argument that most upland cotton was planted on upland cotton base acreage. The amount of acreage planted to upland cotton always remains *below* the amount of upland cotton base acreage – a fact that supports Brazil's assumption that upland cotton producers receive payments related to upland cotton base.⁵⁶

(7) Brazil states that one third of all US farms with eligible acreage decided to update their base acreage under the direct payments and counter-cyclical payments programmes using their MY1998-2001 acreage. What is the proportion of the current base acreage for upland cotton resulting from such updating? Is the observed updating of base acreage consistent with Brazil's argument that it is only profitable to grow upland cotton on base acreage (and peanut and rice base acreage)? BRA

Brazil's Answer:

37. Regarding the first question, Brazil does not know the proportion of current base acreage for upland cotton resulting from the 2002 updating of the base acreage. This information is exclusively collected and maintained by the United States. As indicated in answer to Question 125(5), USDA required all eligible farms to file applications by 1 June 2002 establishing and updating their base acreage. Brazil notes that the United States was quickly able to report that *overall* 99.6 per cent of eligible farms enrolled in the programme. This suggests that the United States is in possession of farm-specific information regarding the percentage of (1) the total amount of upland cotton direct and counter-cyclical payment base acreage, and (2) the number of farms growing upland cotton that chose to update their base acreage. Brazil reiterates its request to the United States for this information.⁵⁷

⁵⁶ Brazil has discussed the validity of this assumption in its answers to Questions 125 (3) and (8).

⁵⁷ Exhibit Bra-49 (Brazil's Questions for the Purposes of Annex V Procedure, March 2003) and Exhibit Bra-101 (Brazil's Questions for the Purposes of the Consultations, 22 November 2002)

38. The answer to the second question is yes. As indicated in Brazil's Answer to Question 125(2)(c), upland cotton producers would lose money in MY 2000-2001 (even with the subsidies) if they grew upland cotton on anything other than upland cotton or rice base acreage. The record indicates that PFC per acre payments were \$30.84 for upland cotton and \$23.48 per acre for corn in MY 2001.⁵⁸ There were no PFC or market loss payments for peanut base under the 1996 FAIR Act.⁵⁹ Testimony from NCC representatives indicated that a number of producers in the south-eastern part of the United States grew upland cotton on corn base acreage during MY 1999-2001.⁶⁰ NCC representatives argued that it would only be "fair" for producers with corn base acreage that had switched into upland cotton production to be able to update their base acreage to receive *upland cotton* direct and counter-cyclical payments.⁶¹ NCC's efforts were successful, as reflected in the fact that under the 2002 FSRI Act, maximum total direct and counter-cyclical per acre payments for upland cotton base acreage is \$109.50, while for corn it is \$54.10 per acre. This large increase in per acre payment for cotton relative to corn in the 2002 FSRI Act reflects the much higher cost of producing upland cotton – and the expectation that historic cotton producers receiving such high payments will continue to grow high-cost upland cotton.

39. Given the much higher per acre payments in MY 2002 for upland cotton base acreage, any producer who could gain more upland cotton base acreage would certainly take advantage of the chance to update. Thus, any increases in the updated upland cotton base in MY 2002 reflect the economic incentive to obtain significantly greater additional revenue by switching to upland cotton acreage than in staying with historical corn, wheat, oats, barley sorghum and barley acreage. Finally, the higher per acre payments for upland cotton also reflect the squeeze in profits for those cotton producers that grew upland cotton in MY 1999-2001 on corn base acreage, as testified to by NCC representatives, discussed above.

(8) How could one take account of upland cotton producers who receive PFC, MLA, direct and counter-cyclical payments for other covered commodity base acreage? BRA, US

Brazil's Answer:

40. The best information to use would be the actual data collected by the United States concerning the amount of PFC, MLA, DP, and CCP payments to US upland cotton producers. In the absence of this information, Brazil's methodology assumes that US producers of upland cotton grew upland cotton on upland cotton base acreage. This is a reasonable proxy, because there will be some upland cotton that is grown on rice (and peanut) base receiving higher payments, and some upland cotton that is grown on, *e.g.*, corn base receiving somewhat lower payments. On average, Brazil's approach would roughly cancel out the *over*-counting of rice and peanut payments and the *under*-counting of corn and any other lower-paying programme crop payments.

⁵⁸ Brazil's 9 October Closing Statement, Annex 1, para. 31, *citing* Brazil's 22 August Rebuttal Submission, paras 32-34.

⁵⁹ Brazil's 24 June First Submission, para. 45; Brazil's 22 August Rebuttal Submission, para. 24

⁶⁰ *See* NCC testimony quoted in Brazil's 24 June 2003 First Submission, para. 53 *citing* Exhibit Bra-41 (Congressional Hearing, "The Future of Federal Farm Commodity Programs (Cotton)," House of Representatives, 15 February 2001, p.32).

⁶¹ "[W]hat has happened is, under Freedom to Farm . . . in the Southeast we moved from corn, like I have done, to cotton. *So the last few years we have increased our cotton acreage in Georgia, for instance, to about a million and a half acres; we are getting [PFC] payments on about 900,000 acres.* [W]e have a tremendous production in the Southeast that is not getting a [Market Loss] payment or a regular [PFC] payment. So we are recommending . . . to this committee that a farmer have a choice with remaining with his existing acreage and yield, *or he has an option to move to a modified acreage and yield on his farm or acreage on his farm, and this would make this, we think, fair.* . . . And this happened . . . outside the Southeast, but it is been more pronounced in the Southeast than any other section of the Country." (emphasis added) Exhibit Bra-41 ("The Future of Federal Farm Commodity Programs (Cotton)," Hearing before the House of Representatives Committee on Agriculture, 15 February 2001, p. 32). Brazil's 24 June First Submission, para. 53.

F. PROHIBITED SUBSIDIES

128. Could the US respond to Brazil's assertions relating to the meaning and effect of the introductory phrase of Article 3 ("Except as provided in the Agreement on Agriculture...")? Would the meaning/effect change if Article 13 of the Agreement on Agriculture did not exist? BRA, US

Brazil's Answer:

41. In commenting on the first question directed to the United States, Brazil notes that the United States argues that the phrase "except as provided in the Agreement on Agriculture" necessarily means that negotiators intended to carve out both domestic local content and export subsidies for agricultural products from the disciplines of Article 3 of SCM Agreement.⁶² But the United States' argument twists the meaning of the phrase "except as provided". The word "except" does not imply that there *must* be something in the Agreement on Agriculture that carves out the disciplines on local content subsidies in the SCM Agreement. The phrase only means that *if* the Agreement on Agriculture clearly and unambiguously (i) exempts such agricultural subsidies from the SCM Agreement, or (ii) changes the obligations contained in the SCM Agreement, then the provisions of the Agreement on Agriculture that conflict with those of the SCM Agreement will prevail. The Appellate Body's jurisprudence teaches that it is only where the text clearly and unambiguously provides for modified obligations does the "except as provided" language become operational.⁶³

42. In essence, what the United States seeks from the Panel is an interpretation that the prohibition on local content subsidies does not apply to agricultural goods. Yet, nothing in the Agreement on Agriculture or the SCM Agreement provides the carve-out the United States now seeks.

43. Brazil agrees that the Agreement on Agriculture constitutes *lex specialis* as opposed to the *lex generalis* of the SCM Agreement. The Agreement on Agriculture applies to a subset of goods covered by the SCM Agreement and, in case of conflicting provisions, the rights and obligations contained therein should prevail over those of the SCM Agreement. Brazil agrees that the introductory phrase of Article 3 of the SCM Agreement makes explicit the *lex specialis* nature of the Agreement on Agriculture.

44. However, the US argument goes further than the principle of *lex specialis derogat generalis* as it is normally applied. The United States wants the Panel to apply this principle in a way that effectively derogates explicit and specific provisions of the SCM Agreement whenever the Agreement on Agriculture is silent about such provisions. This is an absurd application of the *lex specialis* principle. The *lex specialis* is to be read together with the *lex generalis*. In fact, every effort must be made to read the two provisions in a harmonious manner. The derogation of the *lex generalis* is called for only in situations when an irreconcilable conflict between the two texts arises. It is a fundamental tenet of law that absolute contradictions between laws cannot be presumed; they must be established by a systematic analysis of the texts involved to identify any unequivocal incompatibility. Such conflict or incompatibility does not exist with regard to Article 3.1(b) of the SCM Agreement. The Agreement on Agriculture specifies no right or obligation that would, *by necessity*, derogate the obligation contained in Article 3.1(b) of the SCM Agreement. The Appellate Body and panels have

⁶² US 30 September Further Submission, para. 171.

⁶³ Appellate Body Report, *EC – Hormones*, WT/DS26/AB/R, para. 128; Appellate Body Report, *EC – Bananas*, WT/DS27/AB/R, paras. 157-158; Appellate Body Report, *EC – Sardines*, WT/DS231/AB/R, paras. 201, 208.

rightly cautioned against interpretations that would exempt disciplines from entire sections of WTO agreements in the absence of a clear and unambiguous carve-out of rights and obligations.⁶⁴

45. Furthermore, the United States' interpretation, which would (permanently) carve out all agricultural products from the prohibition of Article 3.1(b), is contrary to the object and purpose of Article 3 of the SCM Agreement. Negotiators expressed their intent that local content subsidies are a special class of trade-distorting subsidies. Because of their particularly trade-distortive nature, negotiators dispensed with the requirement of showing any adverse effects and made them prohibited subsidies. Given the special prohibited nature of such subsidies – coupled with the ability of negotiators to carve such subsidies out explicitly from the operation of the SCM Agreement – it would be expected that any exception from the disciplines would be clear and unambiguous.

46. The answer to the second question is “no”. As Brazil's earlier submissions have articulated, Article 13(b) is not the only basis for Brazil's argument that the Agreement on Agriculture does not carve out agricultural local content subsidies from the Article 3.1(b) prohibition of local content subsidies.⁶⁵ As Brazil has argued, there is no inherent conflict between requiring the notification and scheduling of payments to processors of agricultural goods benefiting domestic producers under Annex 3, paragraph 7 of the Agreement on Agriculture and the prohibition on payments to processors of agricultural goods that are contingent upon the use of domestic over imported goods.⁶⁶ Nevertheless, the absence of any reference to Article 3 of the SCM Agreement in Article 13(b) of the Agreement on Agriculture (while a similar reference exists for export subsidies) is consistent with Brazil's other arguments that local content subsidies for agricultural goods are prohibited subsidies.

47. The US interpretation eliminating any prohibitions on agricultural local content subsidies creates a sharp distinction in the way that the other group of normally prohibited subsidies – subsidies contingent upon export – are treated under the Agreement on Agriculture. The Agreement on Agriculture provides many instances in which export subsidies for an individual agricultural product may be challenged as prohibited subsidies under the Agreement on Agriculture. These include prohibitions on export subsidies for unscheduled products, prohibitions on subsidies given to products where support is beyond the scheduled reduction commitments, and prohibitions on subsidies that lead to circumvention of export subsidy reduction commitments. By contrast, under the US interpretation of local content subsidies, there will never be an instance in which local content subsidies for an individual agricultural product would ever be prohibited.

48. It would be expected that such radically different treatment of local content subsidies would be spelled out clearly in the Agreement on Agriculture. Yet, the only link the United States can find to justify its total exclusion of local content prohibited subsidies is the provision in Annex 3, paragraph 7 to include local content subsidies – along with the multitude of other types of domestic subsidies that are *not* prohibited subsidies – in the support to be counted for total AMS. All that Annex 3, paragraph 7 stipulates is that AMS calculations shall include measures that “benefit the producers of the basic agricultural products”. Such language contains nothing that conflicts with the obligation established in Article 3.1(b) of the SCM Agreement. Brazil notes that measures that “benefit the producers of the basic agricultural products” may or may not be “contingent upon the use of domestic over imported good”. In both situations these subsidies must be included in AMS calculations. However, when challenged under the DSU, those subsidies that require local content

⁶⁴ Appellate Body Report, *EC – Hormones*, WT/DS26/AB/R, para. 128; Appellate Body Report, *EC – Bananas*, WT/DS27/AB/R, paras. 157-158; Appellate Body Report, *EC – Sardines*, WT/DS231/AB/R, paras. 201, 208; Panel Report, *India – Quantitative Restrictions*, WT/DS90/R, para. 5.103.

⁶⁵ Brazil's 22 July Oral Statement, paras. 84-86; Brazil's 11 August Answers to Questions, paras. 215-217; Brazil's 22 August Rebuttal Submission, paras. 131-144.

⁶⁶ Brazil's 22 August Rebuttal Submission, paras. 137-140 (setting out examples where no such conflict would exist).

will be found to violate Article 3.1(b) of the SCM Agreement, and the subsidizing Member will be urged to withdraw such measures.

G. SPECIFICITY/CROP INSURANCE

129. In the event that the Panel does not consider that the alleged prohibited subsidies fall within the provisions of Article 3 and are therefore, pursuant to Article 2.3, "deemed to be specific", are there any other grounds on which Brazil would rely in order to support the view that such measures are "specific" within the meaning of Article 2 of the *SCM Agreement* (see, for example, fn 16 of Brazil's further submission)? BRA

Brazil's Answer:

49. Brazil brought prohibited subsidy claims against the Step 2 export and domestic payments, as well as against the CCC export credit guarantee programmes GSM 102, GSM 103 and SCGP. Concerning the latter, only GSM 102 is relevant for Brazil's serious prejudice claims and, thus, the questions of specificity within the meaning of Article 2 of the SCM Agreement only needs to be addressed for that subsidy.

50. Step 2 export and domestic payments are *de jure* specific subsidies because they are only available for exporters and domestic users of upland cotton.⁶⁷ Exporters or domestic users of extra-long staple cotton, any other crop or any other product are not eligible to receive Step 2 payments. Consequently, the United States has notified Step 2 payments as cotton-specific non-green box domestic support.⁶⁸ Thus, Step 2 payments are specific within the meaning of Article 2.1 of the SCM Agreement in much the same way as marketing loan payments or cottonseed payments.

51. Brazil notes that the Panel's question raises a hypothetical situation that is highly unlikely given the clear export contingency of the GSM 102 export credit guarantee programme. Unlike the crop insurance programme, GSM 102 export credit guarantees are available for exports of most US agricultural commodities.⁶⁹ However, GSM 102 support is provided only to enterprises exporting agricultural products and, thus, for the reasons set forth in Brazil's answer to Question 131(a), these subsidies are both *de jure* and *de facto* specific.⁷⁰

130. Does Brazil agree that the US insurance premium subsidy is available in respect of all agricultural products? Please cite relevant portions of the record. BRA

Brazil's Answer:

52. Brazil does not agree that the US crop insurance premium subsidy is available in respect of all agricultural products. At the outset, Brazil would like to clarify that the US crop insurance programme encompasses two different types of subsidies. First, the US Federal Crop Insurance Corporation pays *farmers* a portion of the premiums that they have to pay for obtaining crop insurance.⁷¹ Second, the Federal Crop Insurance Corporation covers losses under crop insurance

⁶⁷ Exhibit Bra-29 (Section 1207(a) of the 2002 FSRI Act) and Exhibit Bra-28 (Section 136(a) of the 1996 FAIR Act).

⁶⁸ See e.g. Exhibit Bra-47 (G/AG/N/USA/43, p. 20). Brazil disagrees with the classification of Step 2 export payments as "domestic support." Brazil also considers Step 2 domestic payments to be prohibited local content subsidies within the meaning of Article 3.1(b) of the SCM Agreement and Article III:4 of GATT 1994.

⁶⁹ See Brazil's Comment to Question 142.

⁷⁰ See Brazil's Answer to Question 131.

⁷¹ Exhibit Bra-30 (Section 508(e) and Section 508(h)(5)(A) of the Federal Crop Insurance Act). Exhibit Bra-59 ("Briefing Room: Farm and Commodity Policy: Crop Yield and Revenue Insurance").

policies that exceed the amount of premiums collected, thus providing free *reinsurance for private insurance companies* offering crop insurance.⁷²

53. Brazil has demonstrated that crop insurance policies that are eligible for subsidy payments – both premium and reinsurance subsidies – are not available in respect of all agricultural products. The United States claims that crop insurance subsidies are and will in the future be available to livestock and dairy producers.⁷³ This assertion is incorrect. First, it is entirely irrelevant if crop insurance will be available to livestock and dairy producers in the future. The question that faces the Panel is whether the US crop insurance subsidies in MY 1999-2002 are specific, not whether they may at some point in the future become less specific. Brazil demonstrated that except for a very narrow pilot programme that began in MY 2002, there were no livestock “crop” insurance policies during MY 1999-2002.

54. Second, Brazil has demonstrated that crop insurance is currently – in MY 2003 – only available to livestock producers in a limited number of US states and counties.⁷⁴ The Adjusted Gross Revenue policy cited by the United States⁷⁵ covers only “incidental amounts of income from animals and animal products and aquaculture reared in a controlled environment,” which must not exceed “35 per cent of expected allowable income”.⁷⁶ In addition, this policy is only available for producers in a limited number of counties in 18 US states.⁷⁷ Even making the entirely unrealistic assumption that *all* US livestock in those pilot counties would be eligible for adjusted gross revenue coverage, that production⁷⁸ would only represent 7.58 per cent of the value of total US livestock production.⁷⁹ In addition, Brazil has demonstrated that the total value of US livestock and dairy production represents 52 per cent of the value of total US agriculture.⁸⁰ Thus, even taking into account the pilot counties for the adjusted gross revenue coverage, at least 48 per cent of the value of US agriculture is excluded from crop insurance subsidy benefits.

55. Third, the 2000 ARP Act itself explicitly limits its application to, *inter alia*, US crops, and does not cover insurance for the production of dairy, beef, poultry, pork and other livestock.⁸¹

56. In sum, the US crop insurance subsidies are not available to all US agricultural production.

⁷² Exhibit Bra-30 (Section 508(k) of the Federal Crop Insurance Act). For the reinsurance agreement standards *see* Exhibit Bra-39 (7 CFR 400.161 et seq.).

⁷³ US 30 September Further Submission, para. 15.

⁷⁴ Brazil’s 7 October Oral Statement, para. 7.

⁷⁵ Brazil notes that this policy is the only one that is cited by the United States in support of its allegation that crop insurance would be available to all US agricultural products. Brazil is not aware of any other policy that would enable and in particular enabled US dairy or livestock producers during MY 1999-2002 to benefit from crop insurance subsidies.

⁷⁶ Exhibit Bra-272 (“Fact Sheet: Adjusted Gross Revenue,” Risk Management Agency, USDA, February 2003, p. 1).

⁷⁷ Exhibit Bra-272 (“Fact Sheet: Adjusted Gross Revenue,” Risk Management Agency, USDA, February 2003, p. 1,3).

⁷⁸ The record shows that most farms are small, and that many small farms specialize in beef production. *See* Bra-285 (“Agriculture Fact Book 2001-2002, Chapter 3 – American Farms, Figures 3.1 and 3.8). Therefore, these farms could not be eligible under the pilot programme because more than 35 per cent of their revenue is generated from the production of livestock. This suggests that even the figure of 7.58 per cent of total US livestock production is a significant overestimate.

⁷⁹ Exhibit Bra-271 (Analysis of the Market Value of Livestock in Adjusted Gross Revenue Insurance Pilot States and Counties).

⁸⁰ Brazil’s 22 August Rebuttal Submission, para. 59 and Exhibit Bra-177 (“ERS Briefing Room: Farm Income and Costs: Farm Income Forecasts”).

⁸¹ Exhibit Bra-30 (Section 518 of the Federal Crop Insurance Act) contains a list of the “agricultural commodities” covered by insurance policies that are subsidized under the Federal Crop Insurance Act.

131. How should the concept of specificity – and, in particular, the concept of specificity to "an enterprise or industry or group of enterprises or industries" -- in Article 2 of the *SCM Agreement* apply to subsidies in respect of agricultural commodities? Please answer the following questions, citing the principles in Article 2 of the *SCM Agreement*: BRA, US

- (a) is a subsidy in respect of all agricultural, but not other, products specific?**
- (b) is a subsidy in respect of all agricultural crops (i.e. but not to other agricultural commodities, such as livestock) specific?**
- (c) is a subsidy in respect of certain identified agricultural products specific?**
- (d) is a subsidy in respect of upland cotton, but not other products, specific?**
- (e) is a subsidy in respect of a certain proportion of the value of total US commodities (or total US agricultural commodities) specific?**
- (f) is a subsidy in respect of a certain proportion of total US farmland specific?**

Brazil's Answer:

57. The short answer to Questions 131(a) – (f) is “yes.”

58. Brazil's Further Submission sets forth a detailed analysis of the legal requirements for *de facto* and *de jure* specificity (paras. 34-40), demonstrating the broad agreement between the official US interpretation of Article 2 of the SCM Agreement in the Statement of Administrative Action (“SAA”) and the position of Brazil. Brazil also provided a detailed application of those requirements for each of the relevant subsidies (paras. 41-70). Brazil offers the following additional comments below:

59. With respect to Question 131(a), a US subsidy that is made available to all enterprises in the industry producing agricultural commodities is specific. As Brazil and the United States agree, the purpose of the specificity requirements is to “function as an initial screening mechanism to winnow out only those foreign *subsidies which truly are broadly available and widely used throughout an economy*”.⁸² The United States' SAA notes that “all governments, including the United States, intervene in their economies to one extent or another, and to regard all such interventions as countervailable would produce absurd results”. Among such “absurd results” would be countervailing “public highways and bridges, as well as a tax credit for expenditures on capital investment even if available to all industries and sectors”.⁸³ After providing these examples, the SAA states that “the specificity test was not intended to function as a loophole through which narrowly focused subsidies provided to or used by discrete segments of an economy could escape the purview of the CVD law”.⁸⁴

60. The US subsidies at issue in this case – including crop insurance – are *de jure* limited under Article 2.1(a) because they “explicitly limit access to a subsidy to certain enterprises”, *i.e.*, those producing, using, or exporting either crops, certain crops, or one crop.⁸⁵ The US subsidies are also *de facto* specific under Article 2.1(c) because they are used by a limited number of enterprises in relation to all enterprises and industries making up the US economy. Only the group of enterprises

⁸² Exhibit Bra-148 (“Statement of Administrative Action,” p. 929).

⁸³ Exhibit Bra-148 (“Statement of Administrative Action,” p. 929-30).

⁸⁴ Exhibit Bra-148 (“Statement of Administrative Action,” p. 930).

⁸⁵ Brazil's 9 September Further Submission, paras. 34-70.

producing agricultural crops is entitled to receive or actually use these subsidies. All other enterprises and all other industries are excluded from the right to receive and, in fact, do not use such subsidies.

61. The broad diversification of the US economy is a relevant fact for the Panel to consider for *de facto* specificity under Article 2.1(c) (“account shall be taken of the extent of diversification of economic activities within the jurisdiction of the granting authority”). The US SAA indicates that the US Department of Commerce should take “account of the number of industries in the economy in question” in “determining whether the number of industries using a subsidy is small or large”.⁸⁶ The US industry growing and producing agricultural products, or even the sub-industry of US producers who grow crops, are in the words of the US SAA, “a discrete segment” of the US economy. The value of all US agricultural production of all commodities is only 0.8 per cent of total US GDP.⁸⁷ Article 2.1(c) requires a Panel to undertake a “case by case” approach to diversification, and Brazil believes the approach presented here and endorsed by the US SAA is an appropriate application of the provision. In the case of the United States, there is a multitude of US industries that do not use the US subsidies at issue in this case. By contrast, in the case of Benin, the agricultural industry represents 38 per cent of its GDP.⁸⁸ For a country like Benin, subsidies to the entire agriculture sector would most likely not be considered to be specific because they are widely available to a large portion of the producers within the economy. No such facts exist for the cotton subsidies at issue in this dispute.

62. Brazil sees no basis in the text of Article 2 of the SCM Agreement for a different specificity test to be applied to subsidies for the purpose of Part V (countervailing measures) and Part III (actionable subsidies) of the SCM Agreement. Nor does Brazil see any basis to apply a different test of specificity for agricultural and other types of goods and industries – no such distinction exists in Article 2 of the SCM Agreement. For example, would a subsidy provided only to the US automotive parts industry (which includes thousands of enterprises) be specific while a subsidy provided to thousands of enterprises producing agricultural crops *not* be specific? There cannot be much doubt that the US automotive parts industry is a discrete segment of the US economy, and a discrete “industry”. Brazil (and the US SAA) is of the view that in both these instances, the subsidy would be specific. All of the US subsidies challenged by Brazil are narrowly focused on, at most, a *portion* of the industry producing agricultural products.

63. With respect to Question 131(b), a subsidy that is provided to enterprises producing all agricultural *crops* is specific. Because the applicable industry is the one producing all agricultural commodities, a subsidy to only enterprises producing crops but not to enterprises producing *other* agricultural commodities is specific. Brazil notes the entirely different approach the United States now asserts in this case, regarding crop insurance, and the official interpretation offered in the SAA.⁸⁹ While the Panel, of course, is not bound by the unilateral interpretation of the United States in the SAA, Brazil believes that the SAA, in this instance, correctly described the intent of the drafters regarding specificity. The producers of US crops are discrete enterprises within a US industry. None of these subsidies is provided to enterprises producing other types of agricultural products that make up approximately 50 per cent of the value of the US agricultural commodities.⁹⁰ In the case of crop insurance, it is useful to recall that many of the small US farming enterprises – representing 92 per cent of US farms – produce livestock, including beef.⁹¹

⁸⁶ Exhibit Bra-148 (“Statement of Administrative Action,” p. 931).

⁸⁷ Exhibit Bra-269 (“Gross Domestic Product by Industry for MY 1999-2001,” Robert J. McCahill and Brian C. Moyer, November 2002, p. 36).

⁸⁸ Exhibit Bra-294 (“The World Fact Book – Benin,” CIA, p.6)

⁸⁹ The “SAA thus contains the view of the Administration, submitted by the President to Congress and receiving its imprimatur, concerning both interpretation and application and containing commitments, to be followed by future Administration, on which domestic as well as international actors can rely.” Panel Report, *US – Section 301*, WT/DS152/R, para. 7.111.

⁹⁰ See Brazil’s Answer to Question 130.

⁹¹ Exhibit Bra-285 (Agriculture Fact Book 2001-2002, Chapter 3 – American Farms, Figures 3.1 and 3.8).

64. In deciding the question, the Panel should also take into account the significant implications of accepting the US arguments that any subsidy provided to all agricultural producers of all agricultural commodities would be non-specific. This interpretation would create a new class of trade-distorting agricultural subsidies that are non-actionable. The United States has always notified its crop insurance subsidies as amber box subsidies, *i.e.*, presumptively trade distorting. And USDA economists have found that even lower subsidies provided by the pre-2000 ARP Act increased US upland cotton acreage by 1.2 per cent and US upland cotton exports by 2 per cent.⁹² Professor Sumner found that the higher subsidies provided by the 2002 ARP Act increased US upland cotton acreage by 3.3 per cent, US exports by 3.8 per cent, and decreased world A-Index prices by 1.3 per cent on average for each year between MY 2000-2002.⁹³

65. The US specificity interpretation would permit, for example, a Member to provide a revenue guarantee to every enterprise producing any agricultural commodity to pay for the total cost of production plus a reasonable profit margin of 10 per cent. The US interpretation would permit Members to make direct payments to every farming enterprise that are tied to a constructed average price index for all agricultural products (not individual prices such as the CCP) and a farmer's current total production. A Member could also provide free inputs for the production of all agricultural commodities to every enterprise producing any agricultural product without that subsidy being actionable under Articles 5 and 6 of the SCM Agreement. In short, if the criteria is, as the United States argues, that the subsidy only need be provided to all farming enterprises, then *any* type of trade distorting non-green box domestic subsidy meeting that universal application criteria would escape discipline under the SCM Agreement.

66. The US interpretation would create a gaping hole in the disciplines of the Agreement on Agriculture and the SCM Agreement. Such an interpretation is clearly inconsistent with the object and purpose of the Agreement on Agriculture, which is to "correct[] and prevent[] restrictions and distortions in world agricultural markets". It is inconsistent with the SCM Agreement's object and purpose of disciplining trade-distorting actionable subsidies. And it is completely inconsistent with the interpretation including in the United States' SAA.

67. With respect to Questions 131(c) and (d), for the reasons set forth above and in Brazil's earlier submissions, a subsidy that is mandated to be provided to only certain enterprises in respect of a handful of identified agricultural products (such as the 10 "programme" crops of the direct and counter-cyclical payment programme) but not provided to most other enterprises within the agricultural industry producing crops or agricultural commodities, is specific under Article 2.1(a) of the SCM Agreement. Similarly, there is *de facto* specificity because these same subsidies covered by the Panel's questions (c) and (d) are only used by certain enterprises of the overall industry producing agricultural commodities (which is the case for all the US subsidies except crop insurance and GSM 102).⁹⁴

68. Regarding Question 131(e), if a subsidy is paid only to enterprises that produce or manufacture products representing a certain *portion* of the value of the products of a single industry (such as the US industry producing agricultural commodities), then the subsidy would be specific. Evaluating specificity based on the "value" of products produced by a single industry is a useful tool for measuring the extent to which the subsidy is provided to discrete enterprises within an industry, or within an economy. When many enterprises in the most highly revenue generating segments of an industry do not receive a subsidy – such as the absence of crop insurance for livestock including beef, poultry and pork, among others – then the subsidy is specific because it is only used by a certain number of enterprises within the industry.

⁹² Brazil's 22 August Rebuttal Submission, paras. 63-64.

⁹³ Brazil's 9 September Further Submission, Annex I, Table 1.5d.

⁹⁴ Brazil's 9 September Further Submission, paras. 41-61.

69. Finally, with respect to Question 131(f), another tool for evaluating the specificity of a subsidy is the amount of total US farmland that receives the subsidy. The use of “farmland” is a rough proxy for the number of enterprises producing agricultural products within the meaning of Article 2.1. For example, only 38 per cent of US farmland is used for the growing of crops (including hay) that are eligible for the payment of crop insurance.⁹⁵ By contrast, 62 per cent of US farmland is used for the production of livestock that, with only a few exceptions, is not covered by US crop insurance. When used in conjunction with the “value” data discussed in Question 131(e) above, this acreage data confirms the fact that a number of enterprises within the industry producing agricultural commodities do *not* receive the crop insurance subsidy. Brazil notes that the United States has not contested the use of similar acreage data to demonstrate the specificity of other US subsidies.⁹⁶

H. EXPORT CREDIT GUARANTEES

137. Please elaborate the meaning of "net losses" as is used in paragraph 70 of Brazil's 7 October oral statement. BRA

Brazil's Answer:

70. The term “net losses” was, in the context of an oral statement, merely a shorthand reference to the elements of item (j) – the provision of the CCC guarantee programmes at “premium rates which are inadequate to cover the long-term operating costs and losses of the programmes”.

71. To prove that the CCC guarantee programmes suffered “net losses” (or in other words meet the elements of item (j)), Brazil referred, in paragraph 70, to the comparison of cohort-specific subsidy figures from the “guaranteed loan subsidy” line of the US budget with cohort-specific reestimates from Table 8 of the Federal Credit Supplement⁹⁷, summed over the period 1992-2002 to determine the performance of the CCC programmes over the long term.

72. Whether starting with the cohort-specific subsidy figure from the budget year column of the US budget or with the cohort-specific subsidy figure from the prior year column of the US budget, the result of this exercise is a positive subsidy number.⁹⁸ The CCC arrives at the very same result in its 2002 financial statements. Specifically, the 2002 financial statements provide a cumulative subsidy figure for *all* post-1991 CCC guarantees, taking account of all adjustments for defaults, fees and reestimates undertaken for all cohorts in all years through 2002. This exercise results in a cumulative

⁹⁵ Exhibit Bra-143 (Agricultural Statistics 2003, National Agricultural Statistics Service, USDA. Table IX-6; *See also* Summary of Business Application, Risk Management Agency. USDA. Accessed 21/10/03, <http://www3.rma.usda.gov/apps/sob/> Based on the 1997 census (the most recent year), the total land in farms is 968,338,000 acres; the total cropland used for crops was 348,701,000 acres; idle cropland and grassland pasture was 580,165,000 acres; the number of acres insured on rangeland, forage seed, forage production, alfalfa seed (*i.e.*, crops that could be grown on grassland pasture) was 12,575,000 acres. If cropland not used for crops was included, then the total amount of acreage not producing insured commodities would be 58.61 per cent and the total amount of acreage used to produce insured (or potentially insured) commodities under the 2002 ARP Act would be 41.39 per cent. Brazil notes that this does not include any reference to the recent pilot programs discussed elsewhere. However, the percentages would not change to any great extent if such acreage were included, given the 35 per cent limit on livestock imposed by the crop insurance program.

⁹⁶ *See* Brazil's 9 September Further Submission, paras. 43-61 (discussion of specificity regarding PFC, MLA, DP, and CCP subsidies).

⁹⁷ Table 8 of the 2004 Federal Credit Supplement is included at Exhibit Bra-182.

⁹⁸ Brazil has offered calculations using the cohort-specific subsidy estimate from the budget year column of the US budget (para. 115 of Brazil's 22 August Rebuttal Submission), and using the cohort-specific subsidy estimate from the prior year column of the US budget (Exhibit Bra-193).

positive subsidy figure of \$411 million for the period 1992-2002.⁹⁹ The Panel will recall that under the Federal Credit Reform Act, when “payments from” the government exceed “payments to” the government on a net present value basis, a positive subsidy results, meaning that CCC is “los[ing] money”.¹⁰⁰

73. Brazil has explained that the FCRA cost formula is one way to determine the performance of the CCC export credit guarantee programmes relative to the elements of item (j). Application of the formula demonstrates that over the period 1992-2002, CCC guarantees under the GSM 102, GSM 103 and SCGP programmes were provided “at premium rates which are inadequate to cover the long-term operating costs and losses of the programmes.”

74. The United States objects to the appropriateness of the FCRA formula as a proxy for the analysis required by item (j).¹⁰¹ The United States’ objection is based on the fact that re-estimates are still being undertaken for all CCC guarantee cohorts during the period 1992-2002. Brazil has therefore also offered a number of other methods to confirm that operating costs and losses for the CCC guarantee programmes outpace premiums collected during the period 1992-2002¹⁰², or in other words, that the CCC guarantee programmes suffered “net losses” over that long-term period.

138. Please comment on Brazil’s views stated in paragraph 70 of its 7 October oral statement. US

Brazil’s Comment:

75. Brazil notes an inadvertent error in paragraph 70 of its 7 October Oral Statement. Exhibit Bra-193 does indeed compare cohort-specific reestimates to cohort-specific subsidy figures from the prior year column of the US budget. However, the comparison of cohort-specific reestimates to cohort-specific subsidy figures from the budget year column of the US budget is reflected in the table at paragraph 115 of Brazil’s 22 August Rebuttal Submission, rather than in Exhibit Bra-192.

76. In Exhibit Bra-192, Brazil subtracted downward reestimates from and added upward reestimates to the original subsidy figure included in the budget year column of the “guaranteed loan subsidy” line of the annual US budget.

139. In the context of export credit guarantees, is the Panel correct in understanding that Brazil's claims of inconsistency with the *Agriculture Agreement* involve GSM 102, GSM 103 and SCGP, but that it limits its "serious prejudice" allegations in respect of export credit guarantee programmes to the GSM 102 programme, and does not challenge GSM 103 and SCGP in this respect? If so,

(a) could Brazil please explain why it did so, and confirm that all the data relied upon in its further submissions (e.g. in Table 13) relate to the GSM 102 programme rather than to GSM 102, GSM 103 and SCGP (and, if the data needs to be adjusted to take account of a narrower "serious prejudice" focus, supply GSM-102-relevant data)? BRA

⁹⁹ Exhibit Bra-158 (US Department of Agriculture, Office of Inspector General, Financial and IT Operations, Audit Report, “Commodity Credit Corporation’s Financial Statements for Fiscal Year 2002”, Audit Report No. 06401-15-FM (December 2002), Notes to the Financial Statements, p. 19).

¹⁰⁰ Exhibit Bra-121 (US General Accounting Office, Report to Congressional Committees, “Credit Reform: US Needs Better Method for Estimating Cost of Foreign Loans and Guarantees,” GAO/NSIAD/GGD-95-31, December 1994, p. 20)). For the FCRA formula, *see* Exhibit Bra-117 (2 U.S.C. § 661a(5)(c)).

¹⁰¹ US 22 August Rebuttal Submission, para. 162.

¹⁰² Brazil’s 11 August Answers to Panel Questions, paras. 163-168; Brazil’s 22 August Rebuttal Submission, para. 109.

77. The Panel is correct in understanding that Brazil's serious prejudice claims involve only GSM 102. All tables and figures that make reference to export credit guarantees in the context of Brazil's serious prejudice claims represent data on GSM 102 only. The reason that Brazil's serious prejudice claims do not cover GSM 103 and SCGP is that either no cotton allocations were made under the programme (GSM 103 for most of the marketing years covered by the period of investigation) or that only negligible amounts of cotton were exported under the programme (SCGP and – if exports took place – GSM 103).¹⁰³ Almost all US upland cotton exports that benefited from a CCC export credit guarantee were covered by the GSM 102 programme. Thus, the only CCC export credit guarantee programme that significantly contributed to the upland cotton-related serious prejudice suffered by Brazil was the GSM 102 programme. Consequently, Brazil has excluded GSM 103 and SCGP from its serious prejudice claims.

78. However, Brazil has included GSM 102, GSM 103 and SCGP in its export subsidy claims under the Agreement on Agriculture and the SCM Agreement. All three CCC export credit guarantee programmes constitute export subsidies within the meaning of Articles 10.1, 8 and 1(e) of the Agreement on Agriculture and Articles 1 and 3.1(a) of the SCM Agreement, and fulfil the criteria of item (j) of the Illustrative List of Export Subsidies attached as Annex I to the SCM Agreement.

(b) for the purposes of Article 13(c)(ii) of the Agreement on Agriculture, is it necessary for the Panel to examine only GSM 102 or should the Panel's examination include also GSM 103 and SCGP? Why or why not? BRA

79. The Panel needs to examine all three programmes under Article 13(c)(ii) of the Agreement on Agriculture. This provision exempts export subsidies from actions based on Article XVI of GATT 1994 and Articles 3, 5 and 6 of the SCM Agreement. Brazil has brought claims under Article XVI of GATT and Articles 5 and 6 of the SCM Agreement against CCC's GSM 102 export credit guarantee programme. Thus, to properly address these claims, the Panel needs to determine whether the GSM 102 programme fully conforms to the provisions of Part V of the Agreement on Agriculture, within the meaning of Article 13(c)(ii) of that Agreement.

80. In addition, Brazil has brought claims under Article 3.1(a) of the SCM Agreement against CCC's GSM 102, GSM 103 and SCGP export credit guarantee programmes. To properly address these claims, the Panel needs to determine whether the GSM 102, GSM 103 and SCGP programmes fully conform to the provisions of Part V of the Agreement on Agriculture, within the meaning of Article 13(c)(ii) of that agreement.

81. To demonstrate that CCC's GSM 102, GSM 103 and SCGP programmes do not fully conform to the provisions of Part V of the Agreement on Agriculture, Brazil has established that GSM 102, GSM 103 and SCGP constitute export subsidies and violate Articles 10.1 and 8 of the Agreement on Agriculture by circumventing or threatening to circumvent US export subsidy reduction commitments. The programmes, thus, do not conform fully to the provisions of Part V of the Agreement on Agriculture.

140. Could Brazil explain how, if at all, it has treated export credit guarantees for the purpose of Table 1 of its further submission? BRA

82. Brazil has not included GSM 102 for the purpose of Table 1 of its Further Submission. While Brazil has demonstrated that GSM 102 export credit guarantees constitute export subsidies within the meaning of the Agreement on Agriculture and the SCM Agreement¹⁰⁴, Brazil is not in a position to quantify the benefit to the recipients that has arisen from the application of the GSM 102 export credit

¹⁰³ Exhibit Bra-73 (Summary of Export Credit Guarantee Programs FY 1999-2003).

¹⁰⁴ Brazil's 22 August Rebuttal Submission, para. 102-110

guarantee programme to exports of US upland cotton between MY 1999-2002. Brazil has no data – nor has the United States provided any – that would enable it to calculate the benefit involved in the GSM 102 transactions.¹⁰⁵

83. However, the National Cotton Council, which represents the industry benefiting from the GSM 102 programme, has provided what appears to be a reasonable estimate of the benefits to US upland cotton producers, users and exporters. These benefits are significant enough to generate an additional 500,000 bales of US upland cotton exports per year and to raise domestic US prices by 3 cents per pound.¹⁰⁶

84. Having proven the export subsidy character of the GSM 102 programme, as well as having proven the production and export-enhancing as well as A-Index-suppressing effects of the programme¹⁰⁷, Brazil has met its burden of proof under Articles 5 and 6.3 of the SCM Agreement and GATT Article XVI to establish that the GSM 102 programme causes serious prejudice to the interests of Brazil.

141. The Panel notes the US argument, *inter alia* in its further submission, that the export credit guarantee programmes are "self-sustaining". Recalling that item (j) of the Illustrative List of Export Subsidies in Annex I of the SCM Agreement refers to "premium rates", could the US expand upon how it takes into account the premium rates for the export credit guarantee programmes in its analysis. US

Brazil's Comment:

85. As Brazil has argued elsewhere, the United States cannot make a showing that the CCC guarantee programmes do not constitute export subsidies by appealing to an *a contrario* interpretation of item (j), since item (j) does not admit of an *a contrario* defense.¹⁰⁸

86. Even if item (j) does admit of an *a contrario* defense, proving that the CCC programmes are "self-sustaining" is not enough. Were an *a contrario* defense possible, it would require the United States to demonstrate that over a period constituting the long term, "premium rates" are adequate to cover operating costs and losses, which include but are not limited to "claims or defaults". In contrast, the United States has argued that it is sufficient to show that "claims or defaults" do not exceed "revenue from whatever source it may be derived".¹⁰⁹ "Revenue from whatever source it may be derived" gives credit to the United States for revenue that is not recognized as relevant for the purposes of item (j), and "claims or defaults" ignores "operating costs and losses" that are relevant for the purposes of item (j).¹¹⁰

87. As a factual matter, Brazil quite evidently does not agree that the premium rates for the CCC programmes meet their long-term operating costs and losses. Brazil has presented voluminous quantitative data demonstrating that long-term operating costs and losses incurred by the CCC programmes outpace premiums collected. Brazil has also provided statements from the USDA Inspector General¹¹¹ and the US General Accounting Office¹¹² establishing that CCC's failure to

¹⁰⁵ However, Brazil has established that GSM 102 guarantees confer benefits *per se*, since there is no comparable commercial instrument available in the marketplace.

¹⁰⁶ See also Brazil's Answer to Question 143.

¹⁰⁷ Brazil's 9 September Further Submission, paras. 184-192.

¹⁰⁸ Brazil's 11 August Answers to Panel Questions, paras. 143-149.

¹⁰⁹ US 11 August Answers to Panel Questions, para. 145.

¹¹⁰ See Brazil's 11 August Answers to Panel Questions, para. 162; Brazil's 22 July Oral Statement, paras. 122-123.

¹¹¹ Exhibit Bra-153 (US Department of Agriculture Office of Inspector General Financial and IT Operations Audit Report of the Commodity Credit Corporation's Financial Statements for Fiscal Year 2000, Audit Report No. 06401-14-FM (June 2001), p. 31 ("[T]he fees CCC charges for its GSM-102 and GSM-103

account for country risk or the credit rating of the borrower in setting guarantee fees means that CCC is charging “premium rates” that do not allow it to cover its operating costs and losses over the long-term.

142. The US has pointed out that there are many limitations on granting export credit guarantees and that there is no requirement to issue any particular guarantee (US further submission, paras 153-156). Can the Commodity Credit Corporation decline to grant an export credit guarantee even in cases where the programme conditions are met? US

Brazil's Comment:

88. No, the CCC cannot decline to grant an export credit guarantee even in cases where the programme conditions are met. The CCC cannot “stem[], or otherwise control[], the flow of” CCC export credit guarantees.¹¹³ The CCC export credit guarantee programmes therefore threaten to lead to (and in fact have led to) circumvention of the United States’ export subsidy reduction commitments, within the meaning of Article 10.1 of the Agreement on Agriculture.

89. Under the Budget Enforcement Act of 1990, the US Office of Management and Budget classifies the CCC export credit guarantee programmes as “mandatory”.¹¹⁴ Mandatory programmes like the CCC export credit guarantee programmes are exempt from the requirement in US law that a programme receive new Congressional budget authority before it undertakes new loan guarantee commitments.¹¹⁵ As the Congressional Budget Office has noted, support *via* mandatory programmes like the CCC export credit guarantee programmes “must be available to all eligible borrowers”, without regard to appropriations limits.¹¹⁶ The Congressional Research Service has similarly stated that “[e]ligibility for mandatory programmes is written into law, and *any individual or entity that meets the eligibility requirements is entitled to a payment as authorized by the law*”.¹¹⁷

90. The fact that the CCC can deny guarantees to individuals who do not meet the eligibility criteria does not, of course, affect the conclusion that CCC cannot “stem[], or otherwise control[], the flow of” CCC export credit guarantees.¹¹⁸ The United States’ FSC measure had eligibility criteria, but

export credit guarantee programmes have not been changed in 7 years and may not be reflecting current costs”). Exhibit Bra-154 (US Department of Agriculture Office of Inspector General Great Plains Region Audit Report of the Commodity Credit Corporation’s Financial Statements for Fiscal Year 2001, Audit Report No. 06401-4-KC (February 2002), p. 49 (“[T]he fees CCC charged for its GSM-102 and GSM-103 export credit guarantee programmes have not been changed for many years and may not be reflecting current costs”).

¹¹² Exhibit Bra-181 (US General Accounting Office, Report to the Ranking Minority Member, Committee on Agriculture, Nutrition, and Forestry, US Senate, “Former Soviet Union: Creditworthiness of Successor States and US Export Credit Guarantees,” GAO/GGD-95-60 (February 1995), p. 135-136). At paragraph 110 of its 22 August Comments on US Answers, Brazil included an extract from this General Accounting Office study demonstrating that CCC’s low premium rates do not allow it to cover its costs and losses, and that the CCC programmes do not meet *non-market*, let alone *market*, benchmarks.

¹¹³ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 149.

¹¹⁴ Exhibit Bra-295 (2004 US Budget, Federal Credit Supplement, Introduction and Table 2 (CCC Export Loan Guarantee Programme classified as “Mandatory” in Table 2, and in the “Introduction”, the Office of Management and Budget states that Table 2 provides “the programme’s BEA classification under the Budget Enforcement Act (BEA) of 1990 as discretionary or mandatory”).

¹¹⁵ See Exhibit Bra-117 (2 U.S.C. § 661(c)(2)).

¹¹⁶ Exhibit Bra-185 (Congressional Budget Office Staff Memorandum, “An Explanation of the Budgetary Changes under Credit Reform”, April 1991, p. 7). See also *Id.*, Table 2, which verifies that the CCC export credit guarantee programmes are “mandatory” programs. Brazil notes that this does not mean that the CCC programmes do not receive appropriations. The United States acknowledges in its 11 August Answer to Question 11 that the CCC programmes receive appropriations.

¹¹⁷ Exhibit Bra-186 (Congressional Research Service Issue Brief for Congress, “Agriculture and the Budget”, IB95031 (16 February 1996), p. 3 (emphasis added)).

¹¹⁸ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 149.

the Appellate Body still concluded that nothing in the measure “stem[ed], or otherwise control[led], the flow of” FSC benefits, leading to a threat of circumvention of the United States’ export subsidy reduction commitments.¹¹⁹

91. The entitlement that qualified applicants have to CCC guarantees is not curtailed by the requirement in US law that CCC not make available guarantees to countries that cannot adequately service debt.¹²⁰ That CCC has the authority to deny guarantees on this basis is not relevant, for at least three reasons.

92. First, under the United States’ FSC measure, US authorities were permitted to undertake a factual enquiry into whether the foreign-source income of the foreign corporation was “effectively connected with the conduct of a trade or business within the United States”.¹²¹ This authority, and the possibility that the factual enquiry could limit the amount of income that would qualify for the FSC exemption, did not prevent the Appellate Body from concluding that nothing in the FSC measure “stem[ed], or otherwise control[led], the flow of” FSC benefits, leading to a threat of circumvention of the United States’ export subsidy reduction commitments.¹²² Similarly, the authority that CCC has to undertake an enquiry into whether particular countries are creditworthy, and the possibility that this enquiry could end up reducing the amount of CCC guarantees, does not prevent a conclusion that nothing “stem[s], or otherwise control[s], the flow of” CCC guarantees. (Brazil notes that, in any event, a conclusion by CCC that a particular country is not creditworthy would not necessarily reduce the threat of circumvention, since nothing prevents CCC from simply reassigning the country’s allocation to a country that is creditworthy.)

93. Second, as Brazil has previously noted, the US General Accounting Office (“GAO”) concluded that the requirement that CCC not make available guarantees to countries that cannot adequately service debt does not remotely curtail CCC’s extension of its guarantees. According to the GAO, “the statute does not place any limit on the amount of guarantees that can be provided each year to high-risk countries in aggregate or individually”.¹²³ Thus, the theoretical possibility to halt support to non-creditworthy countries does not “stem[, or otherwise control[,],” the flow of CCC guarantees.¹²⁴

94. Third, CCC is not concerned enough about creditworthiness to vary its fees based on the country risk involved.¹²⁵ Nor does US law require the CCC to take account of the creditworthiness of *individual guarantee recipients* in the fee charged. In fact, CCC fees expressly do not take account of the credit rating of an individual borrower.¹²⁶ Thus, even if CCC finds a country to be creditworthy, it is not compensated for particularly poor individual credit risks.

95. Nor is the entitlement that qualified applicants have to CCC guarantees curtailed by CCC’s ability to adopt product- and country-specific allocations for its export credit guarantee programmes. Although CCC adopts initial allocations at the outset of a fiscal year, it generously increases those allocations as needed. In its announcement of initial allocations for fiscal year 2004, for example, which extends \$2.8 billion in allocations for CCC guarantees, USDA stated that CCC will subsequently make additional allocations throughout the year that will bring total 2004 allocations to

¹¹⁹ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 12.

¹²⁰ *See* US 30 September Further Submission, para. 154.

¹²¹ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 16.

¹²² Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 149.

¹²³ Exhibit Bra-181 (US General Accounting Office, Report to the Ranking Minority Member, Committee on Agriculture, Nutrition and Forestry, US Senate, “Former Soviet Union: Creditworthiness of Successor States and US Export Credit Guarantees,” GAO/GGD-95-60 (February 1995), p. 7).

¹²⁴ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 149.

¹²⁵ Brazil’s 22 August Comments on US Answers, paras. 109, 112.

¹²⁶ Brazil’s 22 August Comments on US Answers, paras. 109, 112.

more than \$6 billion.¹²⁷ Browsing the archived list of USDA press releases announcing supplemental allocations extended throughout fiscal year 2003,¹²⁸ for example, demonstrates that this is exactly what CCC does – it increases allocations as needed. As noted above, CCC is not required to receive new Congressional budget authority before it undertakes these additional allocations. In fact, Congress requires CCC to make available *at least* \$5.5 billion in guarantees – it does not put a ceiling on the amount to be granted.¹²⁹ The allocation process does not “stem[], or otherwise control[]”, the flow of CCC export credit guarantees.¹³⁰ In fact, it enables CCC to increase the guarantees it can provide.

96. Nor does CCC’s ability to adopt product-specific allocations for its export credit guarantee programmes mitigate the significant threat, under Article 10.1 of the Agreement on Agriculture, that the United States will surpass its agricultural export subsidy reduction commitments by virtue of the CCC export credit guarantee programmes. This threat implicates both unscheduled and scheduled agricultural commodities.

97. For unscheduled products, the ability to adopt allocations is irrelevant. Since CCC export credit guarantees are *available* for unscheduled products¹³¹, the threat of circumvention of the US reduction commitments is tangible, and the United States is in violation of Article 10.1. As Brazil has previously noted, the Appellate Body held that for unscheduled products, it is inconsistent with Article 10.1 to provide *any* export subsidies.¹³² Moreover, the record demonstrates that the threat has materialized, since CCC guarantees have been extended to unscheduled products during, for example, 1999-2003.¹³³

98. For scheduled products, the process of adopting product-specific allocations for CCC export credit guarantee programmes does not mitigate the threat of circumvention – or does not “stem[], or otherwise control[]”, the flow of CCC export credit guarantees – for at least three reasons.¹³⁴

99. First, as the list of allocations included in the programme activity report for fiscal year 2003 demonstrates¹³⁵, most allocations are only made on a country-specific basis, and not on a product-specific basis. In fact, less than 8 per cent of the allocations listed on the 2003 programme activity

¹²⁷ Exhibit Bra-296 (“USDA Announces \$2.8 Billion in Export Credit Guarantees,” FAS Press Release, 30 September 2003).

¹²⁸ See <http://www.fas.usda.gov/excredits/exp-cred-guar.asp>.

¹²⁹ Exhibit Bra-297 (7 U.S.C. § 5641(b)(1); 7 U.S.C. § 5622(a), (b)).

¹³⁰ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 149.

¹³¹ Exhibit Bra-298 (“USDA Amends Commodity Eligibility under Credit Guarantee Programmes”, FAS Press Release, 24 September 2002). Exports of unscheduled agricultural products that are eligible for CCC export credit guarantee coverage include: barley malt and barley extract, corn products, cotton (including cotton yarn, cotton fabric, cotton products, including cotton linters), fish and shellfish, fresh and dried fruits (including apples, apricots, avocados, blueberries, cherries, clementines, dates, figs, grapefruits, grapes, kiwi, watermelons, cantaloupe, honeydew, nectarines, oranges, peaches, pears, plums, prunes, raisins, raspberries, strawberries, tangerines and mixtures thereof), fruit and vegetable concentrates, 100 per cent fruit juices, hay, hides and skins, honey, soybean protein products, vegetables (including asparagus, beans, broccoli, carrots, cauliflower, celery, garlic, lettuce, mushrooms, onions, peas, peppers, potatoes, spinach, squash, sweet corn, tomatoes, and mixtures thereof), wood products (including lumber etc.), wool (including wool fabrics, wool yarn and mohair), worms.

¹³² Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 150.

¹³³ Exhibit Bra-299 (“Summary of FY 2003 Export Credit Guarantee Programme Activity”, USDA, covering GSM-102, GSM-103 and SCGP). For 1999-2002, see also Exhibit Bra-73 (“Summary of Export Credit Guarantee Programme Activity”, USDA, covering GSM 102, GSM 103 and SCGP for US fiscal years 1999-2003).

¹³⁴ See also Brazil’s 24 June First Submission, paras. 300-301.

¹³⁵ Exhibit Bra-299 (“Summary of FY 2003 Export Credit Guarantee Programme Activity”, USDA, covering GSM-102, GSM-103 and SCGP).

report are product-specific.¹³⁶ The press release announcing initial allocations for 2004 contains no product-specific allocations. These allocations do not “stem[], or otherwise control[], the flow of” CCC export credit guarantees in a way that would curb the threat that they will be used to surpass the United States’ export subsidy reduction commitments for scheduled products.¹³⁷

100. Second, the allocations are made on a *monetary* basis, which provides virtually no assurance that the United States will not surpass its *quantitative* export subsidy reduction commitments. This might not happen for all scheduled products in all years, but the threat that it will happen is tangible. Rice provides a good example. Based on the monetary amounts of exporter applications received for the CCC programmes, US export data, and average world prices, CCC guarantees to support US rice exports caused the United States to surpass its quantity export subsidy reduction commitments in fiscal years 2001, 2002 and 2003.¹³⁸ (Even if monetary allocations were relevant, nothing limits the amount of funds that can be allocated. The CCC programmes operate without the constraints of the appropriations process, and Congress requires that CCC make available a *minimum* of \$5.5 billion in export credit guarantees.)

101. Third, the United States’ schedule demonstrates that the CCC export credit guarantees are not the only subsidies available to support exports of scheduled commodities. Combining CCC guarantees with these other export subsidies augments the threat that the United States will exceed its export subsidy reduction commitments.

102. In summary, the CCC cannot “stem[], or otherwise control[], the flow of” CCC export credit guarantees.¹³⁹ None of the factors mentioned by the United States stem the flow of those guarantees, which CCC cannot decline to grant in cases where the programme conditions are met. The CCC export credit guarantee programmes therefore threaten to lead to (and in fact have led to) circumvention of the United States’ export subsidy commitments, within the meaning of Article 10.1 of the Agriculture Agreement.

103. With respect to its claims under the SCM Agreement, Brazil notes that even if the CCC had the discretion not to grant export credit guarantees in cases where the programme conditions are met, it would not affect Brazil’s claim that the guarantees confer benefits *per se*. As Brazil has discussed elsewhere, since CCC export credit guarantees from the GSM 102, GSM 103 and SCGP programmes are unique financial instruments for agricultural commodity transactions that are not available on the commercial market (certainly not for terms longer than the marketing cycles of the eligible commodities), each time they are granted, they confer benefits within the meaning of Article 1.1(b) of the SCM Agreement.

143. Brazil agrees with National Cotton Council estimates of the effects of the GSM 102 programmes (Brazil's further submission, para. 190) but it also cites a different conclusion by Prof. Sumner (paragraph 192). Brazil cites other estimates by Prof. Sumner throughout its further submission. Does Brazil adopt Prof. Sumner's conclusions and estimates as part of its submission? BRA

104. Brazil considers both the National Cotton Council’s and Professor Sumner’s estimates as independent parts of the record that demonstrate the serious prejudice caused by the GSM 102 programme to the interests of Brazil. The NCC has a staff of expert economists (including the former

¹³⁶ Exhibit Bra-299 (“Summary of FY 2003 Export Credit Guarantee Programme Activity”, USDA, covering GSM 102, GSM 103 and SCGP (Total GSM 102, GSM 103 and SCGP allocations for fiscal year 2003 are listed as \$6.025 billion, with product-specific allocations as follows: \$370 million of GSM 102 guarantees to Korea; \$85 million of GSM 102 guarantees to Pakistan; and, \$10 million of GSM 102 guarantees to Tunisia).

¹³⁷ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 149.

¹³⁸ Exhibit Bra-300 (Calculation on US Rice Exports Benefiting from GSM 102, GSM 103 and SCGP).

¹³⁹ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 149.

director of the FAPRI cotton model) and has testified to Congress that the effects of the GSM 102 programme increase annual US cotton exports by 500,000 bales and have a 3-cent per pound price effect.¹⁴⁰ Brazil has no reason to doubt the accuracy and reliability of the sworn NCC testimony to the US Congress.

105. Professor Sumner has based his analysis of the effects of the GSM 102 export credit guarantee programme on the earlier work by the National Cotton Council. Professor Sumner has modelled the impact of the GSM 102 export credit guarantee programme as a shift out of the demand curve for US upland cotton by 500,000 bales.¹⁴¹ Brazil believes that the resulting lower estimates of the effects of the GSM 102 programme offered by Professor Sumner are yet another illustration of the conservative (and reasonable) nature of his model.

106. In response to the Panel's Question, Professor Sumner has rerun the model analyzing the results of a fixed 500,000 bales export effect rather than a shift out of the demand curve by that amount. His original results showed an average annual 305,000 bales export-increasing effect for MY 1999-2002.¹⁴² But the assumption of a fixed 500,000 bale export-increasing effect from the GSM 102 programme results in an average world price effect between MY 1999-2002 of 0.928 cents per pound (or 1.80 per cent) compared to 0.57 cents per pound (or 1.12 per cent) estimated under the previous assumption.¹⁴³ For the period MY 2003-2007 the average world price effect would be 1.07 cents per pound or 1.93 per cent compared to the 0.53 cents per pound or the 0.96 per cent estimated previously.¹⁴⁴

107. Brazil has submitted the analysis of Professor Sumner along with results from other economists and other evidence throughout its submissions. The Panel should consider the complete record in analysing the collective effects of the US subsidies. *Both* the NCC's as well as Professor Sumner's studies are positive evidence of the export-enhancing and price-suppressing effects of the GSM 102 export credit guarantee programme. Both the NCC's testimony as well as Professor Sumner's original as well as revised analysis establishes that GSM 102 causes serious prejudice to the interests of Brazil, within the meaning of Articles 5(c), 6.3(c) and 6.3(d) of the SCM Agreement, and within the meaning of Articles XVI:1 and 3 of GATT 1994.

I. ACTIONABLE SUBSIDIES

145. The Panel notes that different remedies are available in respect of prohibited and actionable subsidies under Articles 4.7 and 7.8 of the *SCM Agreement*. If the Panel were to conclude that a subsidy was prohibited and were to make a recommendation under Article 4.7 of the *SCM Agreement* to withdraw the subsidy without delay, can the Panel:

- (a) also conclude that the same subsidy had resulted in adverse effects to the interests of another Member? If so, what would be the value of such a conclusion in terms of the settlement of the matter before the Panel? BRA, US**

¹⁴⁰ Exhibit Bra-41 ("The Future of Federal Farm Commodity Programmes (Cotton)", Hearing before the House of Representatives Committee on Agriculture, 15 February 2001, p. 12).

¹⁴¹ Brazil's 9 September Further Submission, Annex I, para. 59. For reasons internal to the FAPRI model, Professor Sumner did not include the 3 cents per pound price effect estimated by the NCC in the shift out of the demand curve, thus generating more conservative results. In addition, the implicit supply and demand elasticities used by the NCC imply larger price impacts than those in the FAPRI model used by Professor Sumner, again leading to more conservative results.

¹⁴² See Exhibit Bra-301 (Additional Results from Professor Sumner's Model, Table "Impact of removal of Export Credit (fixed exports)").

¹⁴³ Exhibit Bra-301 (Additional Results from Professor Sumner's Model, Table "Impact of removal of Export Credit (fixed exports)").

¹⁴⁴ Exhibit Bra-301 (Additional Results from Professor Sumner's Model, Table "Impact of removal of Export Credit (fixed exports)").

Brazil's Answer:

108. Regarding the first question, the Panel can conclude that prohibited subsidies have resulted in adverse effects to the interests of another Member. Article 5(c) of the SCM Agreement provides that no Member should cause serious prejudice through the use of *any* subsidy. That includes subsidies that are prohibited under Article 3. Nothing in the text of Articles 4.7 and 7.8 of the SCM Agreement suggests that a complaining party must make a choice between prohibited and actionable subsidy remedies. Brazil has a right to remedies provided by both provisions if the Panel makes the underlying findings that a prohibited subsidy such as Step 2 and export credit guarantees also are actionable subsidies that caused serious prejudice.

109. With respect to the second question, there will be value in the Panel making a recommendation under both Articles 4.7 and 7.8 of the SCM Agreement. A subsidy becomes a *prohibited* subsidy because it is contingent on exports or on the use of domestic over imported goods. If the forbidden contingency is removed, the subsidy may still cause ongoing adverse effects. In addition, there may still be continuing adverse effects from subsidies that were previously contingent on export or local content subsidies. Without a recommendation under Article 7.8, these ongoing as well as continuing adverse effects could not be remedied. Finally, recommendations on both prohibited and actionable subsidy claims may avoid later complications in the event of an appeal of the Panel's final determination.

110. Thus, Brazil urges the panel to make first a recommendation under Article 4.7 of the SCM Agreement that the Step 2, as well as GSM 102, GSM 103 and SCGP export credit guarantee programmes be withdrawn without delay. The Panel should also make a recommendation that the United States remove the adverse effects of the Step 2 and GSM 102 export credit guarantee programmes under Article 7.8 of the SCM Agreement.

(b) take into account the effects of the interaction of those prohibited subsidies with other, allegedly, actionable subsidies? If so, how is this relevant to the issue of causation under Article 5 of the SCM Agreement? BRA, US

Brazil's Answer:

111. With respect to the first question, the text of Article 5 of the SCM Agreement provides that “[n]o Member should cause, through the use of *any subsidy referred to in paragraphs 1 and 2 of Article 1*, adverse effects”. The clear intention is for panels to take into account in assessing adverse effects any and all subsidies that are specific, including those found to be prohibited under Article 3. The only subsidies excluded are those that are not specific. The ban on adverse effects also embraces adverse effects caused by the interaction between all actionable subsidy programmes.

112. Because the Panel is required to examine all actionable subsidies in making its causation determination, it is not appropriate for it to separately analyze the individual effects of each subsidy. Thus, the Panel should look at the interaction of the various types of subsidies at issue and at their *collective* effects. No attribution of the effects to individual subsidies or to prohibited and “other” actionable subsidies is necessary because the remedies of Articles 4.7 and 7.8 of the SCM Agreement are not contradictory.

113. Even if the Panel were to decide that it would be appropriate to examine individual effects of subsidies, Brazil has produced extensive evidence of the link between the serious prejudice caused

and the individual and collective effects of all of the actionable subsidies.¹⁴⁵ If the Panel chooses to examine the individual instead of the collective effects of some of the US subsidies, it can do so based on the evidence produced by Brazil.¹⁴⁶ This evidence establishes causation whether the subsidies are examined individually or collectively. With respect to the interactive effects of the various US subsidies, please see Brazil's Answer to Questions 146.

146. Brazil acknowledges that there are some interaction effects that may increase or decrease the overall effects of the subsidies (Brazil's further submission, para. 225). How would your analysis under Articles 5(c) and 6.3 of the SCM Agreement and Article XVI of GATT 1994 differ if it excluded, for example, crop insurance subsidies, PFC and/or direct payments? BRA

Brazil's Answer:

114. The evidence in the record is more than sufficient to establish present and threat of significant price suppression, increasing world market share, and inequitable share of world export trade even if PFC/direct payments and crop insurance subsidies were not deemed to be actionable subsidies.

115. In response to the Panel's question, Brazil asked Professor Sumner to use his model described in Annex I to Brazil's 9 September Further Submission to eliminate the effects of *all subsidies except the PFC/direct payment and crop insurance subsidies*. Professor Sumner's analysis examined the effects of the remaining US subsidies with respect to a number of factors such as planted acreage, production, US price, adjusted world price etc. The complete set of results is set forth in Exhibit Bra-301.¹⁴⁷ Brazil describes the interactive effects of all US subsidies *except* crop insurance and PFC/direct payments on US export and world A-Index prices below.

116. Analyzing the results for the MY 1999-2002 period from Exhibit Bra-301 shows that *but for* the payments from all US subsidy programmes (except the PFC and crop insurance), US exports would have fallen by 36.81 per cent and the world A-Index prices would have increased on average by 11.00 per cent (or 5.73 cents per pound). When crop insurance and PFC/direct payments are included in the original analysis, US exports fall by 41.17 per cent and A-Index world prices would increase by 12.55 per cent (6.5 cents per pound).¹⁴⁸

117. When the period for MY 2003-2007 is examined, eliminating all subsidies except for crop insurance and direct payments means that, on average, US exports would fall by 37.31 per cent and the A-Index world price would increase by 8.36 per cent (4.63 cents per pound).¹⁴⁹ By comparison, when all US subsidies (including PFC/direct payment and crop insurance) are eliminated, US exports, on average, would decrease by 44.02 per cent and the A-Index price would increase by 10.80 per cent.¹⁵⁰

¹⁴⁵ Brazil's 9 September Further Submission, Sections 3.3.4.7 (individual effects) and 3.3.4.8 (collective effects). *See also* Brazil's 7 October Oral Statement, paras 31-34 (USDA's analysis of individual effects of marketing loan subsidies for cotton for marketing years 2000 and 2001).

¹⁴⁶ The collective and individual effects of the various US subsidies are analyzed by Professor Sumner at Tables 1.5(a) – (e) of Annex I to Brazil's 9 September Further Submission. *See also* Brazil's 9 September Further Submission, Sections 3.3.4.7 (individual effects) and 3.3.4.8 (collective effects). *See further* Brazil's 7 October Oral Statement, paras 31-34 (USDA's analysis of individual effects of marketing loan subsidies for cotton for marketing years 2000 and 2001).

¹⁴⁷ *See* Exhibit Bra-301 (Additional Results from Professor Sumner's Model, Table "Impact of removal of all domestic support except PFC/direct payments and crop insurance")

¹⁴⁸ Brazil's 9 September Further Submission, Annex I, Table I.5a.

¹⁴⁹ *See* Exhibit Bra-301 (Additional Results from Professor Sumner's Model, Table "Impact of removal of all domestic support except PFC/direct payments and crop insurance")

¹⁵⁰ Brazil's 9 September Further Submission, Annex I, Table I.5a.

118. Brazil notes that most of its evidence does not involve proof regarding PFC/direct payments or crop insurance and would, therefore, not be impacted by the assumption in the Panel's question. In addition, many of the econometric analysis cited by Brazil focus on only some of the subsidies challenged by Brazil. The results of these studies are consistent with the findings of Professor Sumner's analysis set out in Annex I to Brazil's 9 September Further Submission and Exhibit Bra-301. In sum, even ignoring the effects of the crop insurance and PFC / direct payment programmes, the US subsidies cause serious prejudice to the interests of Brazil, within the meaning of Articles 5(c), 6.3(c) and (d) and GATT Articles XVI:1 and 3.

148. How should the significance of price suppression or depression be assessed under Article 6.3(c) of the *SCM Agreement*? In terms of a meaningful effect? Or another concept? BRA, US

Brazil's Answer:

119. The significance of price suppression should be assessed by reference to whether it meaningfully affects producers or suppliers of the same product that receives the benefits of the challenged subsidies.¹⁵¹ Price suppression that does not meaningfully affect suppliers or producers of a product cannot give rise to serious prejudice, since it would not be significant. The text of Article 6.3 does not set a numerical limit on the level of price suppression. What renders price suppression significant or insignificant is whether or not it causes adverse effects to the producers or suppliers of the Member(s) concerned, not whether an arbitrary level of numeric significance is achieved.¹⁵²

120. Contrary to the US arguments, there is not an artificial distinction between whether price suppression is "significant" and whether such levels of suppression meaningfully affect suppliers or producers of the product receiving the benefits of the subsidies. Brazil provided considerable evidence setting forth how its producers suffered adverse effects from the levels of price suppression that can be attributed to US subsidies during MY 1999-2002.¹⁵³ A good example of the significance of the levels of price suppression demonstrated by Brazil for MY 2000-2001 is found in the testimony of Christopher Ward. He indicated that a 10-per cent increase in prices for Mato Grosso producers in MY 2000 and MY 2001 would have permitted them to cover their variable costs for MY 2001 and come close to covering variable costs in MY 2000.¹⁵⁴ However, because of the losses they suffered without such revenue increases, many Mato Grosso producers reduced production or were forced out of cotton production – Mato Grosso production fell by 34 per cent between MY 2000-2001.¹⁵⁵

121. The record shows that the adverse effects suffered by Brazilian producers have also been suffered by producers in Africa.¹⁵⁶ Nicolas Minot testified for Benin at the hearing on 8 October. His econometric analysis focused on the effect of lower upland cotton prices on poverty among Benin cotton farmers. Based on his economic analysis, a ten per cent decrease in upland cotton prices drove

¹⁵¹ Brazil's 9 September Further Submission, paras. 251-259; Brazil's 7 October Oral Statement, paras. 30-34.

¹⁵² See also New Zealand's 1 October Further Third Party Submission, paras. 2.21-2.27, tying the analysis of significance under Article 6.3(c) to the notion of serious prejudice to the Member(s) concerned under Article 5(c).

¹⁵³ Brazil's 9 September Further Submission, paras. 444-455 and Annex III.

¹⁵⁴ Exhibit Bra-283 (Statement of Christopher Ward – 7 October 2003, paras. 8-10 and accompanying graph).

¹⁵⁵ Exhibit Bra-283 (Statement of Christopher Ward – 7 October 2003, paras. 8-10 and accompanying graph).

¹⁵⁶ Statement of Mr. Minot. Oral Statement of Benin, 8 October 2003, paras. 29-33 ; Statement of Mr. Ibrahim Malloum, Oral Statement of Chad, 8 October 2003, paras. 13-15.

approximately 83,500 Benin upland cotton farmers below the poverty line.¹⁵⁷ The evidence that African producers have suffered adverse effects by reason of the effects of the US subsidies confirms and supports the evidence presented by Brazil that its producers are suffering adverse effects as well.

122. But even if the Panel decides to adopt some sort of numerical standard not reflected in the text of Article 6.3(c), Brazil has also set forth evidence showing that the levels of price suppression found by a number of different economists are “significant”.¹⁵⁸ In assessing whether the various levels of price suppression found by USDA and other economists are “significant,” the Panel should take into account the fact that upland cotton is a primary commodity traded in huge volumes and produced and consumed in a large number of countries. Under these circumstances, any measurable and identifiable effect on the *world* price from the subsidies provided by a single Member is important. In this case, the Panel is not faced with a difficult decision because during MY 1999-2002 – and even during MY 1997-1998 – the record shows that the absolute numerical levels of price suppression caused by some or all of the US subsidies were significant, ranging from 4 to 26.3 per cent of the world price, and 10 to 33.6 per cent of the US price.¹⁵⁹

153. Would the conditions in Article 6.3(d) of the SCM Agreement be satisfied in respect of time periods other than the one specified? What relevance, if any, would this have for Brazil's claims? BRA

Brazil's Answer:

123. Brazil has demonstrated that the conditions of Article 6.3(d) of the SCM Agreement are fulfilled for MY 2001, 2002 and 2003.¹⁶⁰ The record indicates that the conditions of Article 6.3(d) of the SCM Agreement would also have been fulfilled for MY 1999 and 2000. In addition, the increase in the US share of the world upland cotton market follows a consistent trend. This consistent trend exists whether the Panel analyzes the trend over the period MY 1996-present (described by USDA as constituting a significant change in US farm policy¹⁶¹) or over the period MY 1986-present (since the introduction of the marketing loan programme for upland cotton¹⁶²).

124. The US world market share in MY 2000 was 24.7 per cent, an increase over the previous three-year average (MY 1997-1999) of 23.2 per cent.¹⁶³ Similarly, the US market share in MY 1999 was 24.1 per cent, an increase over the previous three-year average (MY 1997-1998) of 23.4 per cent.¹⁶⁴

125. Further, if the “time period” for assessing a “consistent trend” was changed from 1996-2003 to 1985-2003, the results would not be different. The following figure demonstrates that the increase in the US world market share also follows a consistent trend since MY 1986.¹⁶⁵

¹⁵⁷ Benin's 8 October Oral Statement (Statement of Nicolas Minot, para. 24-25) (estimating that a 40 per cent reduction in price caused 334,000 people to fall below the poverty line, and indicating that smaller reductions in the cotton price cause roughly proportional changes in income, as shown in Table 3 of his paper attached to Benin's 1 October Further Third Party Submission).

¹⁵⁸ Brazil's 9 September Further Submission, Table 22, page 110; Brazil's 7 October Oral Statement, paras. 30-34.

¹⁵⁹ See Brazil's 9 September Further Submission, paras. 148-161, 190, 200-232; 254 Table 23, 379-384. See also Brazil's 7 October Oral Statement, paras. 31-34.

¹⁶⁰ Brazil's 9 September Further Submission, Sections 3.4 and 4.12.2.

¹⁶¹ Exhibit Bra-79 (“US Farm Programme Benefits: Links to Planting Decisions & Agricultural Markets”, USDA, Agricultural Outlook, October 2000, p. 10).

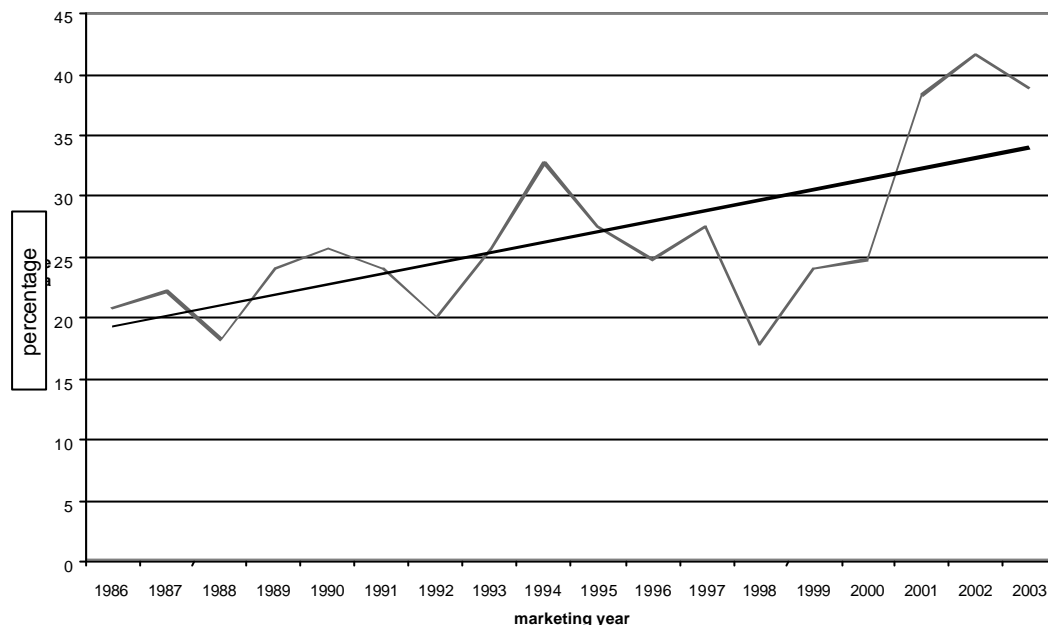
¹⁶² Exhibit Bra-12 (“Cotton, Background for the 1995 Farm Legislation,” USDA, April 1995, p. 15)

¹⁶³ Exhibit Bra-302 (Revised and Extended Data on Article 6.3(d) claim).

¹⁶⁴ Exhibit Bra-302 (Revised and Extended Data on Article 6.3(d) claim).

¹⁶⁵ Exhibit Bra-302 (Revised and Extended Data on Article 6.3(d) claim).

US World Market Share Upland Cotton (MY 1986-2003)



126. The trend line beginning in MY 1986 in the graph above shows an overall consistent increase of US export market share over an 18-year period. This steady long-term increase coincides with the introduction of the marketing loan programme in MY 1986. Another highly trade distortive subsidy, the Step 2 payments, was introduced in MY 1990. The combination of these two subsidies, along with the other trade-distortive subsidies, played an important role in the progressive increase in US world market share over the long-term period covered by the MY 1986-2003 graph above. Thus, looking at all the trends collectively provides corroborating evidence that the large increases in the US world market share from MY 1998 to the present are caused, in significant part, by the US subsidies, in violation of Articles 5(c) and 6.3(d) of the SCM Agreement.

127. Brazil notes that MY 1998 was an unusual year with a relatively low US world market share as a direct result of a 20-per cent abandonment of upland crop acreage due to weather-related issues.¹⁶⁶ But for those weather-related problems, the US world market share would have been higher in MY 1998.

128. Finally, Brazil wishes to correct a typographical error in its calculation of the US world market share for MY 1997. The correct market share (as reflected in Figure 26 of Brazil's 9 September Further Submission) is 27.6 per cent, rather than 19.8 per cent,¹⁶⁷ as was incorrectly noted in Exhibit Bra-206. Brazil notes that this typographical error did not affect the calculations of the increase in the US world market share.¹⁶⁸ Correcting for this error, Brazil resubmits the corrected figures:

¹⁶⁶ See US 30 September Further Submission, para. 19.

¹⁶⁷ The error results from a typographical error in the line of the "total world exports", which were 26.7 million bales in MY 1997 and not 36.7 million bales, as erroneously included in the calculation.

¹⁶⁸ Brazil notes that Figure 26 of Brazil's 9 September Further Submission is unaffected by this data error and shows a very similar trend in the US world market share in cotton.

Figure 25 (para. 270)¹⁶⁹

U.S. World Market Share Upland Cotton (MY 2001)

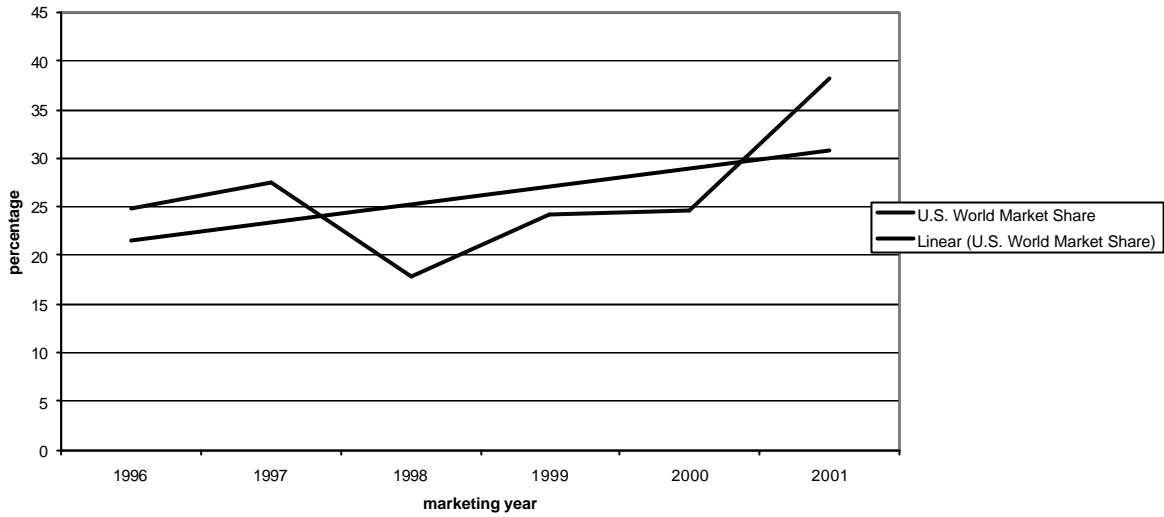
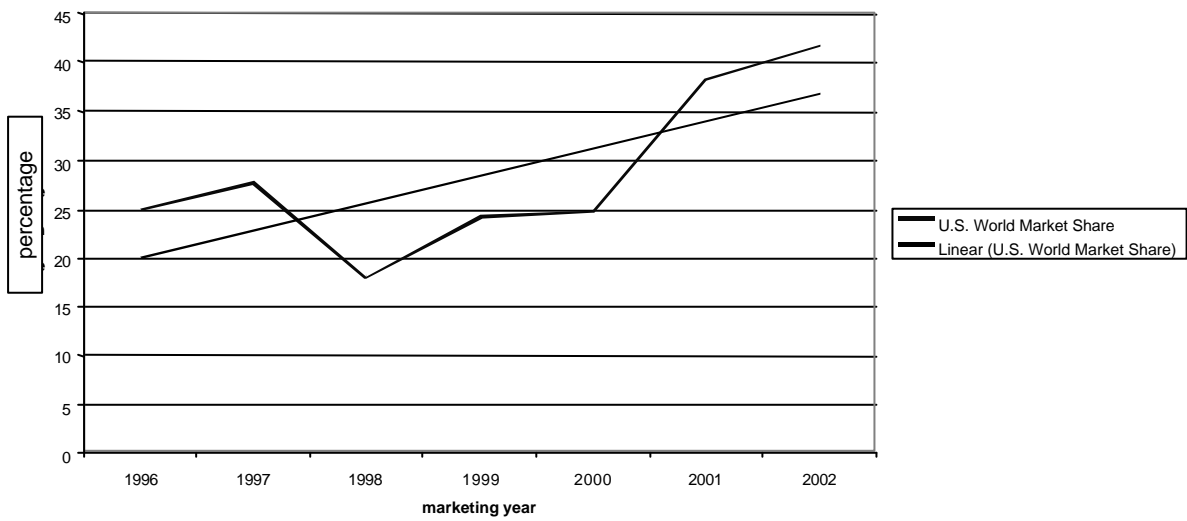


Figure 37 (para. 402)¹⁷⁰

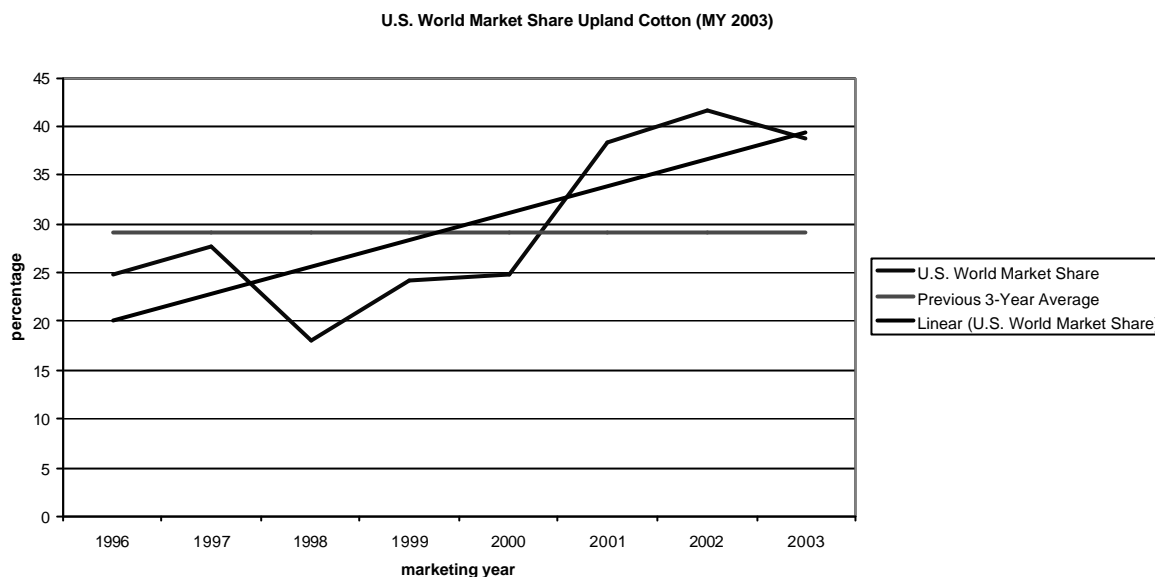
U.S. World Market Share Upland Cotton (MY 2002)



¹⁶⁹ Exhibit Bra -302 (Revised and Extended Data on Article 6.3(d) claim).

¹⁷⁰ Exhibit Bra -302 (Revised and Extended Data on Article 6.3(d) claim).

Figure 38 (para. 405)¹⁷¹



129. As the Panel can see, all three graphs show a trend line that matches the actual curve even better than the trend line presented by Brazil in its 9 September graphs. Also, all trend lines show that there is a dramatically increasing US world market share in upland cotton, in violation of Article 6.3(d) of the SCM Agreement.

161. Would a finding of serious prejudice under Article 5(c) of the *SCM Agreement* be determinative for a finding under Article XVI:1 of the GATT 1994? Why or why not? What, if any, is the role of footnote 13 of the *SCM Agreement* in this context? BRA, US

Brazil's Answer:

130. A finding of serious prejudice based on the effects described in SCM Article 6.3(a), (b), (c) or (d) would be determinative for a finding under GATT Article XVI:1. GATT Article XVI:1 concerns measures that are (i) subsidies, and which (ii) cause or threaten serious prejudice to the interests of any other Member. Footnote 13 of the SCM Agreement provides that “[t]he term ‘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 GATT 1994, and includes threat of serious prejudice”. Footnote 13 clarifies that the instances that constitute serious prejudice within the meaning of the SCM Agreement, including Article 5(c), constitute at the same time serious prejudice within the meaning of GATT Article XVI:1. In addition, if the Panel determines that a particular measure is a “subsidy” under Articles 1 and 2 of the SCM Agreement, that measure would constitute *ipso facto* a subsidy for the purposes of GATT Article XVI:1. In sum, Articles 5(c) and 6.3 of the SCM Agreement operationalize and clarify the meaning of serious prejudice as contained in GATT Article XVI:1.¹⁷²

163. Are US cotton producers able to cover the fixed and variable costs without subsidies? Please provide substantiating evidence. Of what relevance is this, if any, to Brazil's actionable subsidy claims? US, BRA

¹⁷¹ Exhibit Bra-302 (Revised and Extended Data on Article 6.3(d) claim).

¹⁷² This interpretation of the relationship between Articles 5(c) and 6.3 of the SCM Agreement and GATT Article XVI:1 is without prejudice to the continued relevance of GATT Article XVI:3, as discussed in Brazil's answers to Question 185.

Brazil's Answer:

131. Brazil has established in paragraphs 117-123 of its 9 September Further Submission that between MY 1997-2002, US upland cotton producers on average were not able to cover their total cost of production, *i.e.*, the sum of fixed and variable costs.¹⁷³ The gap between the total cost of production and the revenue generated from both upland cotton lint and cottonseed increased steadily from 2.66 cents per pound in MY 1997 to 39 cents per pound in MY 2001 before falling slightly to 34.38 cents per pound in MY 2002.¹⁷⁴ On a percentage basis, the average total costs to produce a pound of upland cotton in the United States between MY 1999-2002 were 77 per cent higher than the average market prices received by US farmers.¹⁷⁵

132. Similarly, the Institute for Agriculture and Trade Policy in Minneapolis found in a study entitled "United States Dumping on World Agricultural Markets" that based on USDA cost of production data, the United States exported its upland cotton below its total cost of production in each year between MY 1990-2001. The study found that US upland cotton was exported between 9 and 57 per cent below the total cost of production.¹⁷⁶ This evidence on export prices is entirely consistent with Brazil's analysis of the gap between total cost of production and farm prices.¹⁷⁷

133. Further, Brazil has used USDA data and the FAPRI 2003 baseline projections on prices and costs of production to analyze the likely gap between total costs of production and market revenues.¹⁷⁸ Based on this information, the gap between total cost of production and market returns to producers of upland cotton will be between 24.85 cents per pound in MY 2003 and 21.85 cents per pound in MY 2007.¹⁷⁹

134. Thus, US producers were not able to meet their total cost of production since MY 1997, and based on USDA and FAPRI baselines, they will not be able to meet their total cost of production through MY 2007. This means that US upland cotton producers would not have met their cost of production for 11 consecutive years absent large US Government subsidies. The average gap between the total cost of production and market return in those eleven years will be 22.85 cents per pound.¹⁸⁰ The only possible conclusion is that many US producers and much US production could not exist without US subsidies, as confirmed by the National Cotton Council.¹⁸¹

135. The consistently large cost-revenue gap, among other factors, establishes the link between US subsidies and increased and maintained high levels of US production and exports. Given the high cost of production that significantly exceeds market revenues, absent the US subsidies, many US

¹⁷³ See also Brazil's Answer to Question 125 (2) (c).

¹⁷⁴ Exhibit Bra-205 (Costs and Returns of US Upland Cotton Producers).

¹⁷⁵ See Exhibit Bra-205 (Costs and Revenues of US Upland Cotton Producers). The number represents the gap between the cost of production of cotton lint and the price received by producers for cotton lint. It does not take into account cottonseed revenue that would slightly narrow the gap.

¹⁷⁶ Exhibit Bra-212 ("United States Dumping on World Agricultural Markets," Institute for Agriculture and Trade Policy, p. 21).

¹⁷⁷ Farm prices are somewhat lower than export prices.

¹⁷⁸ Brazil's 9 September Further Submission, paras. 353-359.

¹⁷⁹ Exhibit Bra-205 (Costs and Returns of US Upland Cotton Producers).

¹⁸⁰ In such a situation it is materially irrelevant whether US producers met their variable cost of production. Meeting at least the variable cost of production may be a short-term option for farmers to stay in business. However, over the long-run, farmers need to cover their total cost of production. Not covering total cost of production for eleven consecutive years would certainly force any producer in any industry out of business.

¹⁸¹ Exhibit Bra-3 (Roger Thurow / Scott Kilman, "US Subsidies Create Cotton Glut That Hurts Foreign Cotton Farms," The Wall Street Journal, 26 June 2002, p. A1) quoting Kenneth Hood, the then Chairman of the National Cotton Council as saying "cotton farmers . . . can't exist without subsidies."

producers would have to cut upland cotton production, and much upland cotton acreage would no longer be planted to upland cotton. This result is intuitively clear and is confirmed by evidence of significant production cut-backs by Mato Grosso producers (34 per cent) who are sensitive to changes in prices, as described in Christopher Ward's statement of 7 October.¹⁸² It is also confirmed by the results of many economists examining the effects of eliminating US subsidies. They found that eliminating the US subsidies that cover the US producer cost-revenue gap would result in lower US production, leading to lower US exports and higher US and world prices.¹⁸³

136. The Panel has also asked for US cost data on variable and fixed costs. Brazil provides below the most recent USDA data covering the period MY 1997-2002.¹⁸⁴ These data demonstrate that the "gross value of the US production" did not permit US upland cotton producers to cover their total costs of production. In MY 2001, the gross value of the production did not even permit them to cover their variable costs of production. In MY 2002, their revenue only covered slightly more than their variable costs. Not reflected in the chart below is the fact that US subsidies made up all (or almost all) the difference between the "gross value of the US production" and the "total costs listed" between MY 1997-2002.

US cotton production costs and returns per planted acre, excluding direct Government payments, 1997-2002 1/

Item	1997	1998	1999	2000	2001	2002
	dollars per planted acre					
Gross value of production:						
Primary product: Cotton	477.48	307.20	274.48	324.33	222.60	257.88
Secondary product: Cottonseed	68.07	48.90	40.32	50.85	48.80	49.95
Total, gross value of production	545.55	356.10	314.80	375.18	271.40	307.83
Operating costs:						
Seed	17.63	17.87	18.35	30.10	37.82	47.99
Fertilizer	35.31	31.76	29.91	31.32	35.26	30.56
Chemicals	60.19	58.54	58.60	58.32	59.25	56.80
Custom operations	23.27	13.02	19.67	19.93	19.99	19.25
Fuel, lube, and electricity	31.64	26.29	26.64	36.97	36.49	31.37
Repairs	25.39	27.32	26.28	27.18	28.53	29.10
Interest on operating inputs	6.57	5.40	5.61	7.55	4.71	2.31
Ginning	62.75	43.78	53.08	51.46	57.14	55.61
Purchased irrigation water	8.71	6.89	6.12	6.55	5.05	5.01
Total, operating costs	271.46	230.87	244.26	269.38	284.24	278.00

¹⁸² See Exhibit Bra-283 (Statement of Christopher Ward – 7 October 2003, para. 6) discussing a drop in the upland cotton acreage in Mato Grosso by 35 per cent between 2000/2001 and 2001/2002 due to low upland cotton prices.

¹⁸³ The collective and individual effects of the various US subsidies are analyzed by Professor Sumner at Tables 1.5(a) – (e) of Annex I to Brazil's 9 September Further Submission. See also Brazil's 9 September Further Submission, Sections 3.3.4.7 (individual effects) and 3.3.4.8 (collective effects). See further Brazil's 7 October Oral Statement, paras 31-34 (USDA's analysis of individual effects of marketing loan subsidies for cotton for marketing years 2000 and 2001).

¹⁸⁴ <http://www.ers.usda.gov/Data/CostsAndReturns/data/recent/Cott/R-USCott.xls>, visited 25 October 2003

Allocated overhead:						
Hired labour	33.72	33.92	35.48	36.98	37.89	38.16
Opportunity cost of unpaid labour	28.03	28.76	29.27	29.90	30.28	32.73
Capital recovery of machinery and equipment	94.21	93.16	96.80	97.97	101.49	100.39
Opportunity cost of land	58.33	46.04	51.84	51.68	43.83	46.76
Taxes and insurance	14.97	14.20	15.07	15.93	16.68	17.01
General farm overhead	15.55	14.21	15.35	15.82	16.11	15.97
Total, allocated overhead	244.81	230.29	243.81	248.28	246.28	251.02
Total costs listed	516.27	461.16	488.07	517.66	530.52	529.02
Value of production less total costs listed	29.28	-105.06	-173.27	-142.48	-259.12	-221.19
Value of production less operating costs	274.09	125.23	70.54	105.80	-12.84	29.83

1/ Estimates based on 1997 survey.

2/ Method used to determine the opportunity cost of land.

J. CAUSATION

165. Please comment (and submit substantiating evidence) on the US assertion that the FAPRI model has been designed and developed for prospective analysis, and is not suitable for retrospective counterfactual analysis. What is the reliability of past FAPRI-produced analyses when compared with actual data for the period covered by them? Is there any other instrument that can be used to try to identify the effect of subsidies already granted, or of their removal? BRA, US

Brazil's Answer:

137. Concerning the first question, there is nothing inherently different in using a calibrated simulation model (the category of models into which the FAPRI and many other models fall) to investigate (i) questions of the future effects on prices and quantities of a potential change in policy or, instead, (ii) questions of how the recent pattern of prices and quantities would have been different if a different set of policies would have been in place. Calibrated simulation models, including the FAPRI model, are routinely used for *both* kinds of questions. The applications are identical. In one case, the comparison for the results from the counter-factual policy option is to an unobserved future baseline. In the other case, the comparison for the results from the counter-factual policy option is retrospective to past actual events.

138. The FAPRI policy simulation framework is an elaborate set of supply and demand equations (along with associated stock equations and equilibrium conditions that set quantity supplied equal to quantity demanded). The framework includes, as a component, a set of "baseline" projections of agricultural prices and quantities for future periods that are based on explicit assumptions about policy, climate, technological change, macroeconomic conditions, etc. In many applications, the relevant questions investigated by the model are of the following form: if some specific policy were different in the future, how would this affect the future outcomes for farm commodity prices and quantities. For example, this is the form of question that is often posed in the context of options for changing US farm subsidies in the future. Because they have baseline projection components, the FAPRI framework and a few others are well suited for these future-oriented questions. But the use of such models to analyze the recent past is also common whenever that is a relevant question.

139. As with other calibrated simulation models, the FAPRI model itself is also used routinely for both projections *and* retrospective counterfactual analysis. One recent publication that applied retrospective counterfactual analysis concerned world peanut (groundnut) policy. That study adapted the basic FAPRI framework, much as it was adapted to apply to the current case for upland cotton, to consider international peanut policy questions. The model is calibrated to three recent years – 1999/2000, 2000/2001 and 2001/2002 – and examines a peanut trade liberalization scenario.¹⁸⁵

140. A second recent retrospective counterfactual application was to the US sugar programme in a project conducted for the US General Accounting Office. In that analysis, a version of the FAPRI domestic sugar model was combined with the CARD international sugar model (much as Professor Sumner has done for upland cotton, as reported in Annex I to Brazil's 9 September Further Submission). The model was calibrated to 1999 data, and results considered the effects of policy reform relative to the 1999 crop year actual outcomes.¹⁸⁶

141. In addition, Brazil notes that USDA has frequently used calibrated simulation models to perform retrospective, counterfactual analysis. For example, USDA economists calibrated the USDA "SWOPSIM" model, which was used extensively to analyze trade policy options in the 1980s and 1990s, to 1989 data and solved it for commodity prices and quantities that would have obtained in that year under alternative trade liberalization scenarios.¹⁸⁷

142. The USDA "FAPSIM" model, which is quite similar to the FAPRI model, is a calibrated simulation model that is also used for retrospective counterfactual analysis and for considering policy options relative to projections. According to J. Michael Price of the USDA Economic Research Service, who was one of the developers of the model and currently maintains and operates the model, it is calibrated to historical data each year as well as to the official USDA baseline. That model is used for responding to questions about future policy options *and* to retrospective counterfactual questions. Indeed, one of the first published applications of the "FAPSIM" model was a retrospective counterfactual analysis of US grain storage policy.¹⁸⁸

143. One of the most recent applications of the USDA "FAPSIM" model was to respond to requests for both alternative projections and retrospective counterfactual analysis from the *Commission on the Application of Payment Limitations for Agriculture*. These results, which have been discussed in previous submissions by Brazil, used the FAPSIM policy framework.¹⁸⁹

144. According to the Commission Report (chaired by the Chief USDA Economist):

"Westcott and Price analyzed the effects of eliminating marketing loans on production and prices of major crops over the period from 1998 through 2005. The

¹⁸⁵ Exhibit Bra-303 (John C. Beghin and Holger Matthey. "Modeling World Peanut Product Markets: A Tool for Agricultural Trade Policy Analysis." Center for Agricultural and Rural Development (CARD), May 2003).

¹⁸⁶ Exhibit Bra-304 (John C. Beghin, Barbara El Osta, Jay R. Cherlow, and Samarendu Mohanty. "The Cost of the US Sugar Programme Revisited," Center for Agricultural and Rural Development (CARD), March 2001).

¹⁸⁷ See <http://www.ers.usda.gov/data/sdp/view.asp?f=trade/92011/> and <http://www.ers.usda.gov/data/sdp/view.asp?f=trade/92012/>.

¹⁸⁸ Exhibit Bra-305 (Larry Salathe, J. Michael Price and David Banker. "An Analysis of the Farmer Owned Reserve Program 1977-82." American Journal of Agricultural Economics, February 1984, p. 1-11).

¹⁸⁹ See Brazil's 7 October Oral Statement, paras. 31-34.

baseline used for the analysis was the USDA 2000 baseline, which did not anticipate the sharp decline in cotton price for 2001 crop year.”¹⁹⁰

...

“The Commission requested that the above study be updated to take into account the sharp decline in cotton prices for the 2001 crop (Westcott). The updated analysis indicated that elimination of marketing loan benefits for the 2001 crop would have lowered cotton acreage by 2.5 to 3.0 million acres or 15-20 per cent and reduced rice acreage by 300,000 acres or 10 per cent.”¹⁹¹

145. Finally, there are literally hundreds of other academic and government studies using a variety of models calibrated on retrospective data that analyze policy questions. All computable general equilibrium models use this approach, and most academic partial equilibrium simulation models do so as well.

146. Concerning the second question, it is difficult to determine the reliability of the analysis of *potential* (i.e., future) policy outcomes because – by definition – the baseline approach will not mirror exactly the actual conditions. This is why baseline projections use long-term data to even out inevitable fluctuations in commodity market developments. Similarly, the *but for* analysis of a retrospective study attempts to simulate what would have (but did not actually) occur with different policy assumptions. However, the retrospective analysis has the benefit of using actual market data and not projected benchmarks. It is, of course, possible to critique selected portions of the FAPRI baseline projections if they are treated as forecasts of the future values for prices and quantities. Against this benchmark, the FAPRI projections – like all others – will sometimes miss future movements in commodity markets.

147. One measure of the reliability of the FAPRI baseline is that the FAPRI model continues to be relied upon regularly by a variety of US government and US industry organizations to guide decisions on important policy questions. USDA even provided the FAPRI economists with their highest award based on the 2002 baseline analysis.¹⁹² In addition, FAPRI economists over the years have performed checks to ensure that the FAPRI model is as reliable as possible. For example, observed (actual) planted acreage has generally responded in the directions the model projects when the loan rates and other driving factors are relatively constant. In addition, FAPRI constantly examines the internal consistency of the model and its economic logic when compared to actual market events and conditions and makes appropriate adjustments, as necessary.

148. Concerning the third question, there are a number of other potential simulation modelling frameworks that can be used as instruments to respond to retrospective counterfactual policy questions. The USDA FAPSIM model is one such framework. It was used, for example, in the Westcott/Price analysis of the effect of removing all marketing loan payments for MY 2000 and MY 2001.¹⁹³ However, the FAPSIM model does not have a full international cotton model as used in the

¹⁹⁰ Exhibit Bra-276 (Report of the Commission on the Application of Payment Limitations for Agriculture, August 2003, p. 124).

¹⁹¹ Exhibit Bra-276 (Report of the Commission on the Application of Payment Limitations for Agriculture, August 2003, p. 125). See further: Westcott, Paul C. “Marketing Loans and Payment Limitations.” Presentation to the Commission on the Application of Payment Limitations for Agriculture, May 2003 as cited in the Payment Limitations Report; Exhibit Bra-222 (Westcott, Paul C., and J. Michael Price. Analysis of the US Commodity Loan Program with Marketing Loan Provisions. USDA, ERS Agricultural Economic Report 801, April 2001); Westcott, Paul and Mike Price. Estimates done at the request of the Commission on the Application of Payment Limitations for Agriculture utilizing the Economic Research Service’s FAPSIM model, 2003 as cited in the Payment Limitations Report.

¹⁹² Brazil’s 9 September Further Submission, Annex I, para. 4 (last sentence).

¹⁹³ See Brazil’s 7 October Oral Statement, paras 32-33.

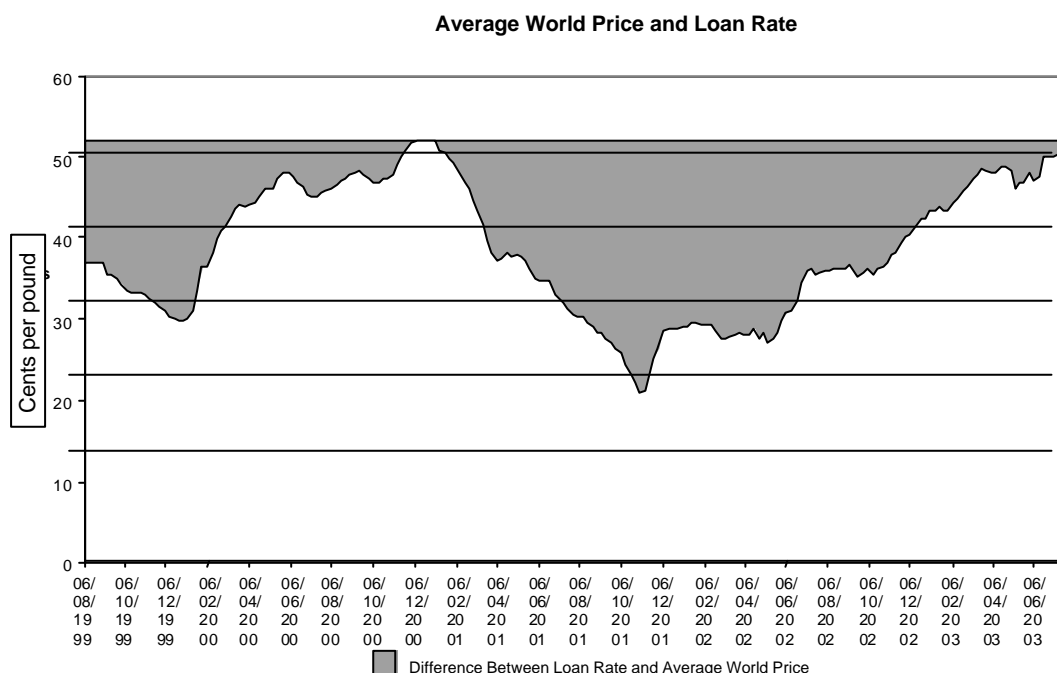
FAPRI/CARD framework, and thus would be less appropriate for dealing with the world price aspects of this case. In general, for specific questions about how quantities and prices of upland cotton would have been different but for US upland cotton subsidies, the appropriate models with which Brazil is familiar would all follow the same basic simulation framework as the FAPRI model.

167. How does Brazil react to Exhibit US-44? BRA

Brazil's Answer:

149. The United States claims that Exhibit US-44 demonstrates the “disconnect between the decline in cotton prices ... and the incentive offered by US marketing loans.”¹⁹⁴ But all that Exhibit US-44 does is to show monthly A-Index prices for upland cotton. These prices, as with other primary agricultural commodities, move up and down with large swings. This exhibit provides no insight into the link between US producer’s decisions to keep planting upland cotton as upland cotton prices (including A-Index prices) move up and down. Further, the quantity of subsidies provided by the US marketing loan is a function of the difference between the loan rate (currently 52 cents per pound) and the adjusted world price (AWP) for upland cotton – not the A-Index price.¹⁹⁵ As the Panel can see from the chart provided in response to Question 181, the AWP is consistently and considerably below the A-Index.

150. A relevant graph to examine the causal link between US subsidies and US production is one with a horizontal line representing the marketing loan rate, and which compares that line against the AWP, which is the basis for the payment of marketing loans. This is illustrated in the graph below:¹⁹⁶



151. This graph shows first what the Exhibit US-44 neglected to illustrate – that except for a short period in MY 2000, the AWP was *below* the loan rate throughout *all* of MY 1999-2002, and that marketing loan payments corresponding to the difference between the AWP and the loan rate were

¹⁹⁴ US 7 October Oral Statement, para. 23.

¹⁹⁵ See Brazil’s Answer to Question 180.

¹⁹⁶ The data is based on the data collected for Brazil’s Answer of Question 181, *see* Exhibit Bra-311.

made. All of the dark area below the 52 cents line represents marketing loan subsidies paid to US upland cotton producers. This illustrates US producers' indifference to market prices. To paraphrase the United States, the line of 52 cents per pound illustrates a "disconnect," but it is not one between the A-Index price and US subsidies. Rather, this graph illustrates the disconnect between the AWP (and more importantly, the US price received by upland cotton producers) and the acreage and production response of US producers: even when prices go to record lows, US producers' revenue is insulated from the decline. This revenue not only kept them in production, but it allowed them to *increase* production during MY 1999-2001. And more remarkably, it kept many of the producers planting 14.2 million acres of cotton when the AWP was near record lows in the period from February-June 2002. These low prices during the crucial planting decision period are clearly reflected in the figure above.¹⁹⁷ It was this period that USDA economists Westcott and Price examined and found that but for the marketing loan payments in MY 2001, US upland cotton production would be 2.5-3 million bales less than it actually was.

152. Thus, this graph helps explain why there is such a limited response from high-cost US upland cotton producers to changes in upland cotton prices. Of course, the graph above does not represent the full amount of revenue supplied by all US subsidies. Other programme features and other programmes provide additional subsidies that cause the effective per unit revenue guarantee to be much higher than the loan rate.

153. If the purpose of Exhibit US-44 was to demonstrate the absence of a link between US upland cotton production (and price suppression) and US marketing loan payments, then it flies in the face of the findings of USDA's own economists. Brazil has referenced the testimony of USDA's chief economist, among many other USDA economists, who have candidly acknowledged the enormous production and price effects that US marketing loan subsidies have on stimulating and maintaining large amounts of US upland cotton production.¹⁹⁸

170. Brazil quotes a report that states that a 10 per cent increase in soybean prices reduces upland cotton acreage by only 0.25 per cent (Brazil's 7 October oral statement, para. 27). Could Brazil indicate if this analysis is done on a short-run basis or a long-run basis? BRA

Brazil's Answer:

154. The authors of the USDA study cited by Brazil – USDA economists Westcott and Meyer – use a “modified version of the estimated elasticities from Lin et al.,”¹⁹⁹ which Westcott/Meyer refer to as a technical improvement. The original study by Lin et al. appears to estimate short to medium-run elasticities. Lin et al. use what they describe as “new supply response elasticities . . . in short-term, acreage forecasting applications”.²⁰⁰ For the estimation of the elasticities themselves, Lin et al. use two models that are solved by regression analysis of the effect of expected relative price changes between crops and the resulting acreage effects in the two following years.²⁰¹

¹⁹⁷ See Brazil's 7 October Oral Statement, paras. 32-33.

¹⁹⁸ Brazil's 9 September Further Submission, paras. 148-161. See further Brazil's 7 October Oral Statement, paras 31-34.

¹⁹⁹ Exhibit Bra-275 (“US Cotton Supply Response Under the 2002 Farm Act,” Westcott and Meyer, USDA, 21 February 2003, p. 9). Brazil is not in a position to specify in which sense the estimated elasticities are modified.

²⁰⁰ Exhibit Bra-306 (“Supply Response under the 1996 Farm Act and Implications for the US Field Crops Sector,” Lin et al., USDA, July 2000, p. 2).

²⁰¹ Exhibit Bra-306 (“Supply Response under the 1996 Farm Act and Implications for the US Field Crops Sector,” Lin et al., USDA, July 2000, p. 9-16).

155. Lin et al. present their results in Table 21 of their study.²⁰² It appears that the resulting estimates of the acreage price elasticities are short or medium-term elasticities (acreage reaction one to three years in the future), and that the adaptations by Westcott and Meyer are also short to medium-term elasticities.²⁰³

172. Please estimate the price effect, in cents per pound, of the growth in the US retail market which it is said has directly contributed to strengthening world cotton prices. US

Brazil's Comment:

156. Brazil emphasizes that its claims under Article 6.3(c) of the SCM Agreement revolve around the present and threatened suppression of prices. Thus, whether world upland cotton prices are strengthening or weakening is irrelevant to the question whether those prices would have been higher (at any price level) *but for* the US subsidies.

176. With reference to Figure 4 of Brazil's Further Submission, how does Brazil explain the apparent decrease in prices in 2001 and the increase of the A-Index in recent months, despite the continued use of US subsidies on upland cotton? BRA

Brazil's Answer:

157. Brazil has consistently argued that over the period of investigation (MY 1999-2002), the US subsidies caused price suppression that was significant when A-Index prices declined and when A-Index prices increased both during and near the end of the period of investigation in mid-2003.²⁰⁴ As Brazil explained at the meeting on 7 October 2003, A-Index prices rise and fall for a variety of supply and demand reasons.²⁰⁵ One of the reasons that prices fell as low as they did in MY 1999-2001 and did not rise as far as they should have in MY 2002 was due to the US subsidies. This is best illustrated in Figure 14, set out in Brazil's 9 September Further Submission and reproduced below:

²⁰² Exhibit Bra-306 ("Supply Response under the 1996 Farm Act and Implications for the US Field Crops Sector," Lin et al., USDA, July 2000, p. 60).

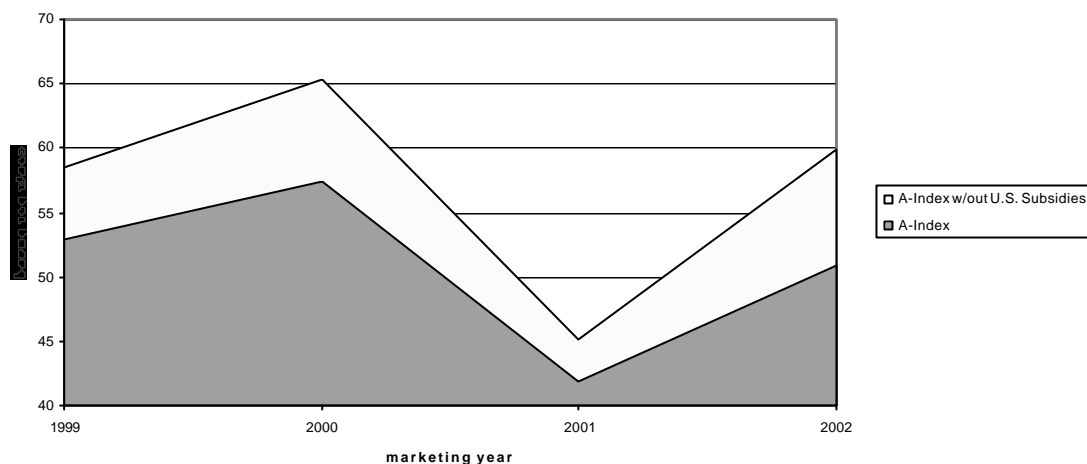
²⁰³ Due to the adaptations, the elasticities reported by Westcott and Meyer are not identical to those reported by Lin et al.

²⁰⁴ Brazil's 9 September Further Submission, paras. 83-89 (discussing definition of "price suppression"); paras. 92-93 (discussing "causation").

²⁰⁵ Brazil's 7 October Oral Statement, paras. 18-28.

Figure 14²⁰⁶

Price Suppression MY 1999-2002



158. This figure represents Professor Sumner’s findings, but a similar figure could be reproduced to reflect other levels of price suppression – including the 33.6 per cent suppression of US prices found by USDA’s own economists for MY 2001,²⁰⁷ as well as the ICAC and other international organizations’ findings of price suppression caused by US subsidies for upland cotton.²⁰⁸ Professor Sumner’s findings indicate that during MY 1999-2002, there were a number of global supply and demand factors (including \$12.9 billion in US subsidies) that caused upland cotton prices to fall and remain at low levels compared to historical prices throughout the period of investigation. The upper line on the graph reflects the contribution of the \$12.9 billion in US subsidies to keeping A-Index prices suppressed. The area below the upper line and above the darker area reflects the amount of price suppression. In other words, regardless of whether market prices rise or fall, there is always a price-suppressive effect.

159. With respect to the Panel’s specific question regarding the effects of US subsidies in the latter half of MY 2002, the record shows that US and A-Index prices rose in MY 2002 for a number of supply^{and} demand factors – many of which also impacted the market during the fall of prices in MY 1999-2001. The most important supply factor was the *decline* in production of 1.71 million tons in MY 2001-2002 by non-US producers such as the African Franc zone, Southern Africa, East Asia, South Asia, and the former Soviet Union countries.²⁰⁹ The evidence suggests that many of these producers could not maintain existing levels of production at lower prices that existed in MY 2001 and MY 2002. For example, Christopher Ward testified that even though Brazilian Mato Grosso producers had extremely high yields and low costs, they were forced by low prices to cut their production by 34 per cent in 2001 and by 25 per cent in 2002, compared with 2000 production levels.²¹⁰ Similarly, Mr. Ibrahim Malloum, President of CottonChad, testified that lower prices in MY

²⁰⁶ A-Index prices with and without subsidies are based the baseline and the change from the baseline as reflected in the results of Professor Sumner’s simulation model. See Brazil’s 9 September Further Submission, Annex I, Table I.5a.

²⁰⁷ Brazil’s 7 October Oral Statement, para. 32-33.

²⁰⁸ See Brazil’s 9 September Further Submission, paras. 148-162 (discussing price suppressing effects of marketing loan payments including Figure 11 at paragraph 160), para. 190 (NCC estimates of 3 cent per pound price suppressing effect from only the GSM 102 program), paras. 200-213 (various international studies), paras. 214-232 (Professor Sumner’s analysis). See also Brazil’s 7 October Oral Statement, paras 31-34 (discussion of Westcott/Price studies of price suppressing effects of marketing loans in MY 2000 and MY 2001).

²⁰⁹ Exhibit Bra -208 (“Cotton: World Statistics,” ICAC, September 2003, p. 28-29).

²¹⁰ Exhibit Bra -283 (Statement of Christopher Ward – 7 October 2003, para. 6).

2001-02 meant that Chadian production fell because producers could not afford inputs such as fertilizer.²¹¹

160. For US producers at the time of planting for the MY 2002 crop – between January-April 2002 – the AWP and US price received by US producers were near record lows.²¹² Faced with an annual 39 cents per pound differential between total costs and such prices in MY 2001, US cotton producers still planted 14.2 million acres of upland cotton for MY 2002.²¹³ The resulting US production in MY 2002 was 16.73 million bales (or 3.64 million metric tons). This is an extraordinary amount of acreage and production given the huge gap between US producers' costs and expected *market* revenue. It is estimated that without US subsidies, US production in MY 2002 would have been approximately 1.92 million metric tons, or 1.72 million metric tons less than what US upland cotton farmers actually produced.²¹⁴ The effects of this additional 1.72 million metric tons of subsidy-generated production can be judged from the effects of an *actual* decline in world supply of 2.365 million metric tons²¹⁵, which contributed to an *increase* in A-Index prices of 33 per cent between MY 2001 and MY 2002.²¹⁶ If an *additional* 1.72 million metric tons of US production were taken out of world supply, prices would have been even higher. Professor Sumner has indicated that A-Index prices in MY 2002 would have increased by 17.70 per cent absent the US subsidies.²¹⁷ Thus, the effect of the US subsidies in MY 2002 – even as prices increased – was to suppress prices.

178. The Panel notes Exhibit US-63. Could the US please provide a conceptually analogous graph concerning US export sales during the same period? US

Brazil's Comment:

161. Brazil offers a conceptually analogous figure to Exhibit US-63 concerning US and rest-of-the-world export sales. The figure below shows the relative changes in US and non-US exports as compared to the previous year for the period MY 1997-2002, based on data covering the period MY 1996-2002.²¹⁸

²¹¹ Chad's 8 October Oral Statement (Statement of Ibrahim Malloum, para. 7).

²¹² See Brazil's Answer to Question 167.

²¹³ Exhibit Bra-4 ("Fact Sheet: Upland Cotton," USDA, January 2003, p. 4).

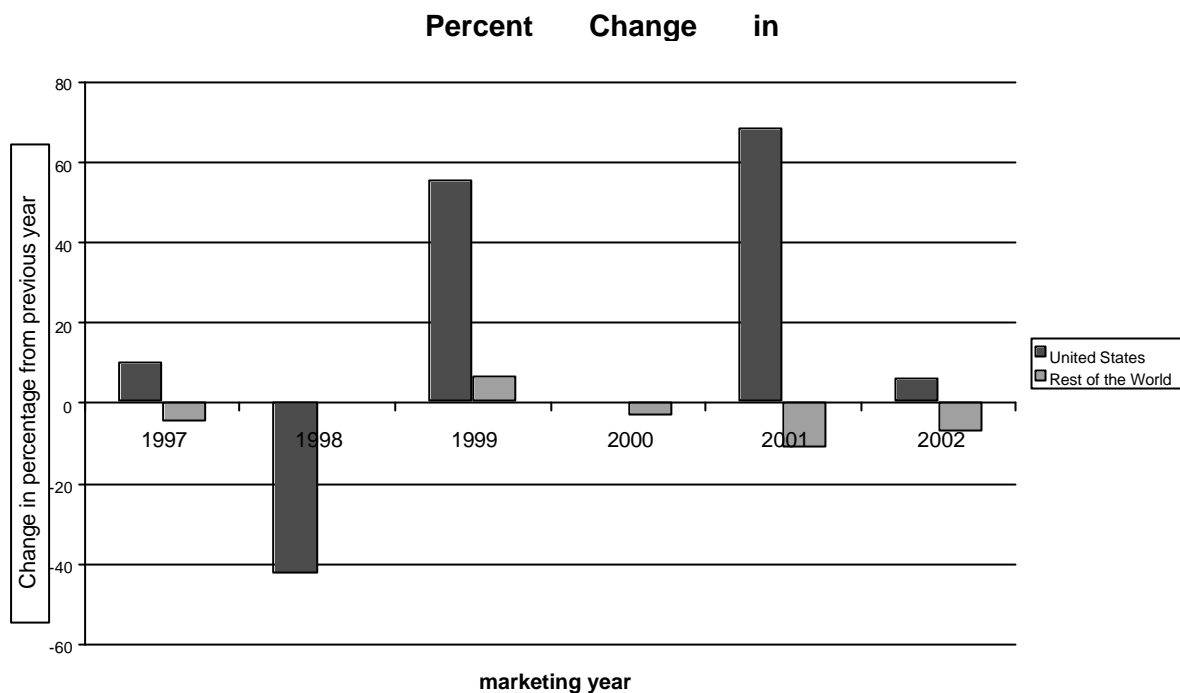
²¹⁴ Brazil's 9 September Further Submission, Annex I, Table I.5a applying the percentage change.

²¹⁵ Exhibit Bra-208 ("Cotton: World Statistics," ICAC, September 2003, p. 4).

²¹⁶ Exhibit Bra-208 ("Cotton: World Statistics," ICAC, September 2003, p. 106).

²¹⁷ Brazil's 9 September Further Submission, Annex I, Table I.5a.

²¹⁸ Exhibit Bra-307 (Change in US and World Exports in Percent). The exhibit also contains the underlying data for the figure with the sources being described in more detail in Exhibit Bra-302 (Revised and Extended Data on Article 6.3(d) claim).



162. The figure demonstrates that US exports increased in every year except for MY 1998, during which the United States claims it suffered a major crop failure. In addition, US exports increased in all years, except for MY 1998, more than exports from non-US producers, which since MY 2000 even *decreased* continuously. The figure demonstrates that the United States gains world market share, with its own exports increasing since MY 1999, at the expense of non-US exports, which have fallen since MY 2000.

163. In sum, this figure supports Brazil’s claim of serious prejudice under Articles 5(c) and 6.3(d) of the SCM Agreement. It also supports Brazil’s claim of serious prejudice under Articles XVI:1 and 3 of GATT 1994 because the USshare of world export trade increased, in significant part, by the US subsidies at the expense of other lower-cost producers.

179 Could Brazil comment on the argument that decoupled payments and other subsidies to upland cotton are largely being capitalized into land values and that removing these subsidies would reduce the cost of production of upland cotton producers (US 7 October oral statement, para. 48). What would be the net effect of these adjustments? BRA

Brazil’s Answer:

164. A February 2003 study by ERS economists estimated that “decoupled” payments lead to an increase of about 8 per cent in US farmland values.²¹⁹ A more comprehensive ERS 2001 report estimating the regional effects of all subsidies (not just decoupled subsidies) on land values found that land values increased by 16 per cent in the regions where upland cotton is grown. This is shown in the following chart:²²⁰

²¹⁹ Exhibit Bra-308 (“Decoupled Payments: Household Income Transfers in Contemporary US Agriculture,” ERS Agricultural Economic Report No. 822).

²²⁰ Exhibit Bra-309 (Barnard C., Nehring, R., Ryan, J., Collender, R. “Higher Cropland Value from Farm Programme Payments: Who Gains?” Economic Research Service. USDA Agricultural Outlook November 2001, p. 29).

**ERS/USDA Estimated Cropland Value Attributable to
Commodity Programme Payments**

Region	Total Value of Land Harvested in 8 Programme Crops	Estimated Value Attributable to Commodity Programme Payments	Per cent of Value Attributable to Commodity Programme Payments
Prairie Gateway	41.70	9.40	23.00
Mississippi Portal	17.30	2.70	16.00
Fruitful Rim	21.60	2.20	10.00
Southern Seaboard	18.20	1.80	10.00
Eastern Uplands	4.60	0.50	10.00
Total	103.40	16.60	16.05

165. Brazil notes that neither of these studies provides an estimate of the percentage of each dollar of “decoupled” or total subsidy payments that are capitalized into land *values*. However, an August 2003 study by ERS economists indicates that PFC payments in MY 1997 resulted in an increase of land rents by 34-41 cents of per PFC dollar.²²¹ Thus, contrary to the premise of the Panel’s question, this evidence suggests that PFC payments are somewhat, but not “largely capitalized” into land rents.

166. There would be only a minimal impact on total costs of production for upland cotton farmers from the removal of both “decoupled” and total US subsidies. For the allegedly “de-coupled” payments referred to in the February 2003 ERS study, the impact of an 8 per cent reduction in land values translates into a decrease in total costs of US upland cotton producers by less than one per cent (0.75 per cent).²²² If the effects on increased land values from all subsidies are taken into account (using the 2001 ERS regional study), then US upland cotton producers’ costs would have declined between MY 1999-2002 by only 1.49 per cent.²²³ In response to the Panel’s question, the net effect of these tiny adjustments throughout MY 1999-2002 on the very wide cost-revenue gap and the other costs of production analysis conducted by Brazil in its various submissions is obviously minimal.

167. Finally, the United States at paragraph 48 of its 7 October Oral Statement criticized Professor Sumner’s analysis for allegedly not factoring into his estimates the effect of direct payments being capitalized into increased land rents. The US criticism is misplaced. Professor Sumner’s model used very low estimates of production incentives for every dollar of PFC payments (only 15 per cent) and direct payments (only 25 per cent).²²⁴ By taking a very conservative approach for these direct payments, Professor Sumner’s analysis more than allows for the effects these payments have in increasing land values. This can be illustrated by using the 34-41 per cent results of the August 2003 land rent study referred to above. The results of this study suggest that 66-59 cents of each PFC dollar are *not* reflected in increased rents. This leaves more than enough residue from each PFC and direct payment dollar to account for the only 15-25 per cent production effects for PFC/direct payments found by Professor Sumner.²²⁵

180. Please describe the precise formula as to how USDA determines the "adjusted world price" using the Liverpool A-Index, the NY futures price and any other relevant price indicators. Please submit substantiating evidence. BRA, US

²²¹ Exhibit Bra-310 (“The Incidence of Government Program Payments on Agricultural Land Rents: The Challenges of Identification”, Roberts, Kirwan, and Hopkins, August 2003, American Journal of Agricultural Economics, p. 767.).

²²² Exhibit Bra-7 (ERS Data: Commodity Costs and Returns).

²²³ Exhibit Bra-7 (ERS Data: Commodity Costs and Returns).

²²⁴ Brazil’s 9 September Further Submission, Annex I, para. 48.

²²⁵ Brazil’s 9 September Further Submission, Annex I, para. 48.

Brazil's Answer:

168. Brazil looks forward to receiving a detailed description of the complicated calculation of the adjusted world price from the United States in reply to this question. Brazil has set forth a brief description of the calculation of the adjusted world price in paragraph 73 of its 24 June First Submission, and will elaborate to the best of its understanding.

169. The details of the complicated calculation method for the adjusted world price are laid down in 7 CFR 1427.25.²²⁶ The weekly *Cotton Outlook* published by Cotlook Ltd. provides a somewhat simpler description of the process. Exhibit Bra-51 includes the Cotton Outlook description of the "US Pricing Mechanism", including the calculation of the adjusted world price for the week of 31 January 2002.²²⁷

170. The descriptions shows that the adjusted world price is calculated based on the A-Index from which a total adjustment factor is subtracted, thus:

The Adjusted World Price (AWP) is calculated from CIF North Europe quotations, adjusted for shipping, location and quality differentials. The Shipping Differential is derived from the average over the preceding 52 weeks, or as many of that number of weeks for which quotations are available, of the difference, calculated from Thursday's values only, between the average of the Memphis and California/Arizona CIF North Europe quotations, and the Middling 1-3/32" (31-35) domestic spot market average. However, the Shipping Differential in any week may not fall below, or rise above 115 per cent, of an assessed actual transportation cost (now 12.9 cent). A further discount, the Course Count Adjustment, is applied by reference to the amount by which the World Quality difference exceeds the appropriate Loan Quality Difference. It applies to cotton of any grade stapling 1-1/32" or shorter, and to selected lower grades in longer staples.²²⁸

171. Brazil also notes that under certain conditions, the Secretary of Agriculture is entitled to reduce the adjusted world price below the result of this calculation – the so-called Step 1 adjustment. In such circumstances, the adjusted world price would be reduced by a maximum of the difference between the A-Index and the average of the cheapest US Middling 1-3/32" CIF North Europe quotes – thus, the amount by which the US price quotes exceed the average of the five cheapest price quotes worldwide. Such a downward adjustment would increase the amount of marketing loan payments that US upland cotton farmers receive and help close the cost-revenue gap that US producers face.

181. Please provide a side -by-side chart of the weekly US adjusted world price, the Liverpool A-Index, the NY futures price, and spot market prices from 1996-present. What, if anything, does this reveal? BRA, US

Brazil's Answer:

172. In Brazil Bra-311, Brazil provides a side-by-side chart of the weekly US AWP, the A-Index, the nearby New York futures price, the average US spot market price and prices received by US producers from January 1996 to the present. The figure below shows the respective price developments over this period. Exhibit Bra-311 also contains a colour copy of this chart.²²⁹

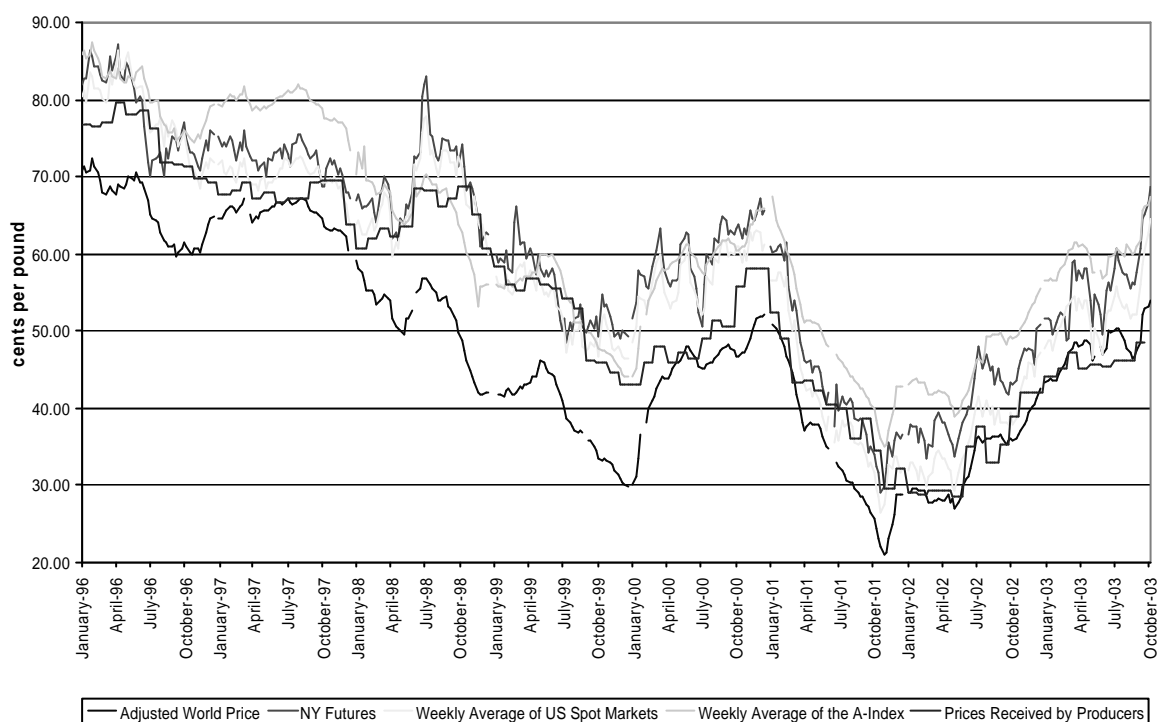
²²⁶ Exhibit Bra-36 (7 CFR 1427.25).

²²⁷ Exhibit Bra-51 (Cotton Outlook, 1 February 2002, p. 16).

²²⁸ Exhibit Bra-51 (Cotton Outlook, 1 February 2002, p. 16) (emphasis in original).

²²⁹ The data has been obtained from the Cotton Outlook published by Cotlook, Ltd. in Liverpool.

Upland Cotton Prices: 1996 - Present



173. The figure demonstrates that the A-Index price is consistently 12-14 cents per pound higher than the adjusted world price (“AWP”), which constitutes the basis for the US marketing loan payments. The average difference between both prices over the 1996-present period is 13.76 cents per pound. As expected, both prices move in parallel. Further, both prices follow the price trends that originate from the New York futures market or at least move in parallel to those prices. There is also a close linkage between the average US spot market price and the New York futures and A-Index prices.

174. The figure further demonstrates that the New York futures prices and the average US spot market prices are usually more volatile than the A-Index and AWP prices. Thus, any rapid increases or decreases in the New York futures prices will not necessarily be reflected to the same extent in AWP or prices received by US producers – the prices of which marketing loan and counter-cyclical payments, respectively, are triggered. They may just be a temporary phenomenon.

175. In sum, the price movements support Brazil’s argument that New York futures, US and international prices for upland cotton are closely linked, and that price movements and trends originating from the US market are closely tracked by prices on the world markets.²³⁰

176. That US and international – and indeed Brazilian – prices closely track each other demonstrates that production and price effects from the US subsidies on the US market are transmitted to the international upland cotton market and to third country markets such as the Brazilian market or markets where Brazil exports its upland cotton. The Panel will remember that the A-Index is composed of price quotes from 16 different upland cotton export markets around the world.²³¹ Thus, if USDA studies like those undertaken by Westcott and Price establish price-suppressing effects of the US subsidies for the US market, those effects will also occur on the

²³⁰ See Section 3.3.4.9 of Brazil’s 9 September Further Submission, para. 233-250.

²³¹ Brazil’s 9 September Further Submission, Annex II, para. 24.

international and third country markets. The parallelism in the price movements establishes the link between price suppression in the US and international markets and other third country markets.

182. Please explain why the US can be taken to be price leaders, or price setters, (and not just takers) when US producers receive large subsidy payment to support the difference between world prices and their own costs? BRA

Brazil's Answer:

177. The Panel's question focuses first on "US producers" who receive large subsidies. One of the premises of this question is that US producers receive subsidies that account for the difference between *world* prices and their own costs. This is not entirely correct. US producers receive what the USDA refers to as "Average price received by US producers". During the MY 1999-2002 period, this US producer price was on average 9.2 cents per pound, or 17.6 per cent, *below* the world A-Index price.²³² Other than the first month of marketing year 1999, the A-Index price was always higher than the US price received by US producers between MY 1999-2002. The lower prices paid to US producers are partly explained by the transportation costs of upland cotton from the United States to foreign markets, where most US upland cotton is marketed. However, as the Panel's question suggests, the total revenue received by US producers includes marketing ban payments that are a function of the set loan rate (52 cents in MY 2002) and the adjusted world price that itself is determined in part by reference to the A-Index prices.

178. During MY 1999-2002, individual US producers of upland cotton did not "set" or "lead" A-Index prices. Most US producers were isolated from the effects of market price during MY 1999-2002. As the Panel's questions implies, on average, US producers were generally able to cover their costs based on a combination of market revenue and the large subsidies they received during MY 1999-2002.²³³ The guaranteed subsidies and price support at high price levels ensured a revenue stream that left them largely indifferent to market prices throughout the entire period of investigation.

179. The Panel's question further asks how the United States could be a "price setter" in the world upland cotton market. Individual US *exporters* of US upland cotton do not "set" or "control" the price of upland cotton. In a world-wide market such as the upland cotton market, no single private trader has the market power (in an anti-trust sense) to "set" the world price. As Andrew Macdonald testified, prices of upland cotton are *discovered* hourly and daily by traders in the futures, spot, and forward delivery markets based on key supply and demand factors.²³⁴ Nor has Brazil argued that the US *leads* prices down by initiating a price war, as may occur with industrial products.

180. What Brazil has argued is that the United States is a leading *driver* of the world upland cotton market to the extent it suppresses the price of upland cotton. The United States can do this because of its large guaranteed production and direct subsidies that inject a near permanent stream of large US production and supplies into the world market. US export subsidies drive the world market in the sense that they stimulate the demand for high-cost US upland cotton at the expense of other world producers. Further, its size (by far the largest exporter and second largest producer), its transparency, which in turn plays a major role in the price discovery in the New York futures market, and the ability of US exporters to use the Step 2 and GSM 102 tools to market US upland cotton, allow it to suppress world prices.²³⁵ Only by taking these price-suppressing factors into account could it be said that the United States "leads" world prices.

²³² See Brazil's Answer to Question 181 for data on the A-Index prices and the prices received by US producers.

²³³ See Brazil's Answer to Questions 125 (2) (c) and 163.

²³⁴ Brazil's 9 September Further Submission, Annex II, paras 11-13, 15-25 and 38-42.

²³⁵ Brazil's 9 September Further Submission, paras. 134-145; Annex II, paras. 38-42 and Chad's 8 October Oral Statement (Statement of Ibrahim Malloum), para. 13-14.

181. For example, the large size of the US production, which represents approximately 20 per cent of total world supply annually, is a key factor in driving and influencing world prices.²³⁶ Shifts in US production caused by good or bad US weather influence total world supply and create an impact on world prices.²³⁷ In much the same way as US weather plays a role in the discovery of world prices (by reducing US and, thus, world stocks), continued high levels of US production generated by US subsidies suppressed world prices throughout the period of investigation by increasing world supplies.

182. Further, the dominant (over 40 per cent) export market share of the United States coupled with the Step 2 and GSM 102 export subsidies creates a further suppressing effect on world prices.²³⁸ These export subsidies allow US exporters to price their upland cotton below the prices of most other world producers because Step 2 gives them (not US producers) the difference between the lowest US price and the A-Index price (the average five lowest prices in the world market).²³⁹ These subsidies, along with the domestic production and direct payment subsidies, have permitted exporters of high-cost US upland cotton to increase US world market share even as prices plunged throughout MY 1999-2001. Thus, while individual US exporters may not have “set” or “led” prices, the US subsidies allowed these exporters to continue marketing high-cost US cotton at *whatever* market price was determined by global supply and demand conditions.

K. ARTICLE XVI OF GATT 1994

183. Why does Brazil believe that the appropriate "previous representative period" is the term of the previous Farm Bill, MY1996-2002? (Brazil's further submission, para. 282) BRA

Brazil's Answer:

183. The Panel's question has stimulated a re-evaluation by Brazil of the appropriate “previous representative period” in relation to Article XVI:3. Brazil agrees with the US arguments made in the *EEC – Wheat Flour* GATT dispute that the appropriate “previous representative period” in Article XVI:3 should be one in which trade patterns have not been distorted by subsidies. In that dispute, the United States correctly argued:

...that the three most recent calendar years could not be used as the representative period in the case since, given the distortion of trade patterns resulting from the heavy use of export subsidies by the EEC, it did not constitute a period during which “normal market conditions existed.” There was ample GATT precedent for selecting a period when subsidization was not unduly affecting the market shares. During the 1995 Review Session it was agreed that in determining what is an equitable share of world trade, the CONTRACTING PARTIES should not lose sight of the “fact that

²³⁶ Brazil's 9 September Further Submission, para. 135.

²³⁷ Consider the following market reports: Exhibit Bra- 312 (Cotton Outlook, 4 October 2002, p. 3 (“Current developments on the production side – though perhaps not the consumption side – would seem to be constructive for prices. Yield potential in several parts of the world appears to be diminishing as a result of unfavourable weather – including storm systems affecting open cotton in parts of the United States.”)); Exhibit Bra-312 (Cotton Outlook, 27 September 2002, p.3 (“Tropical Storm Isidore drove New York futures to higher levels earlier this week, on the grounds that its predicted path would bring heavy rainfall across a huge swathe of the south eastern United States and the Memphis Territory, and thus damage yield and quality prospects... [D]espite the adverse weather, the US will continue to need to make inroads into what remains a significant exportable surplus.”)); and Exhibit Bra-312 (Cotton Outlook, 7 June 2002, p. 3 “Many eyes are directed towards developments in West Texas, where rain appears to have fallen too heavily in places where it is less needed and insufficiently in the dryland areas where soil moisture is lacking.”)).

²³⁸ See Brazil's 9 September Further Submission, paras. 139-142.

²³⁹ Chad's 8 October Oral Statement (Statement of Ibrahim Malloum), para. 14; Brazil's 9 September Further Submission, Annex II, paras. 31, 49-53.

the export subsidies in existence during the selected representative period may have influenced the share of the trade obtained by the various exporting countries.” (GATT, BISD 3rd Supplement, paragraph 19, page 226). Then, in 1960, the CONTRACTING PARTIES adopted a Panel Report which dealt with notification of subsidies, in which it was agreed that an analysis of the effect of a subsidy should include statistics “... for a previous representative year, which were possible and meaningful, should be the latest period preceding the introduction of the subsidy or preceding the last major change in the subsidy.” (GATT, BISD 9th Supplement, Annex II(b)(ii), page 194)... Thus, *it was necessary to examine a period of which preceded the adoption of the EEC’s subsidy system in order to assure that the trade distorting effect which the EEC system had already had on world markets was minimized as a factor in judging “equitable share.”*²⁴⁰

184. There has been no period since the 1930s when US producers of upland cotton were not subsidized.²⁴¹ Since the 1980s in particular, US upland cotton producers have been guaranteed very high levels of government payments by a variety of subsidies, including the marketing loan programme that began in MY 1986. The revenue guarantee that these subsidies provide has locked in large amounts of apparently permanent high-cost US upland cotton production and exports. These distortions exist even in those years in which actual quantities of payments under the programmes are minimal due to higher prices. This is because the subsidies provided to high-cost producers in years of low prices mean they stay in business to continue to produce upland cotton also at times when subsidies fall due to increased prices. The relatively small planted acreage and production response by US producers to market prices over many years reflects the effects of this guaranteed US government revenue.

185. In view of the US arguments in *EEC – Wheat Flour* and the long-term distortions in the US production and exports caused by US subsidies, one appropriate “representative period” would be a simulated period in which no subsidies were provided. The Panel would examine the question: what would be a Member’s share of world trade if it received no subsidies? This question, of course, is a function first of the amount of acreage and production, and ultimately exports attributed to the subsidies. The Panel is fortunate to have the benefit of very recent 2003 analysis by USDA economists Westcott and Price, who estimated that up to 3 million US acres of upland cotton production would have not been planted in MY 2001 if no marketing loan payments were made that year. These 3 million acres represent 19.36 per cent of US upland cotton acreage in MY 2001.²⁴² A reduction by this amount would imply a reduction in US production of 3.79 million bales for MY 2001.²⁴³ Consequently, US exports would also fall by about 3.79 million bales, representing 34.74 per cent of US exports in MY 2001.²⁴⁴ The implied export effects from the Westcott/Price study are very similar to those found by Professor Sumner, who estimated the export-increasing effects of the marketing loan programme in the comparable period to be 29.67 per cent and the effects of all US subsidies to increase US exports by 48.16 per cent.²⁴⁵

186. The record provides an example of what the US share of world export trade in upland cotton would be in a marketing year in which production and exports fell by amounts similar to those estimated by Professor Sumner and Westcott/Price. In MY 1998, 20 per cent of US upland cotton

²⁴⁰ GATT Panel Report, *EEC – Wheat Flour*, para. 2.8 – 2.9 (emphasis added).

²⁴¹ See Brazil’s 9 September Further Submission, para. 269.

²⁴² Exhibit Bra-4 (“Fact Sheet: Upland Cotton,” USDA, January 2003, p. 4).

²⁴³ 19.36 per cent of 19.603 million bales as reported in Exhibit Bra-4 (“Fact Sheet: Upland Cotton,” USDA, January 2003, p. 4).

²⁴⁴ Exhibit Bra-4 (“Fact Sheet: Upland Cotton”, USDA, January 2003, p. 5).

²⁴⁵ Brazil’s 9 September Further Submission, Annex I, Tables I.5d and I.5a. See paras. 17-18 and 75 for determining the comparable period.

acreage was abandoned and US harvested acreage fell by 2.8 million acres compared to MY 1997.²⁴⁶ US production fell by 4.77 million bales and US exports fell by 3 million bales. As a result, US world market share declined from 27.6 per cent in MY 1997 to 17.9 per cent in MY 1998.²⁴⁷ This considerable decrease in the US share of world export trade provides an approximation for the Panel to assess what the equitable US share would be *but for* the US subsidies in MY 2001-2003. Thus, MY 1998 is a useful representative period for the Panel to examine (in conjunction with Professor Sumner's and USDA economists Westcott/Price's analysis).

187. An alternative representative period that the Panel could use for assessing the *inequitable* nature of the US share of world export trade in upland cotton is the period MY 1994-96, during which the average level of US subsidies fell to "only" \$495 million per year.²⁴⁸ The development of the US world market share in MY 1994-1996 compared to MY 2001-2003 is shown in the graph below:²⁴⁹



188. During the period 1994-1996, US producers were generally able to cover their total costs of production largely from market revenue. In these conditions, US world market share averaged 28.4 per cent.²⁵⁰ Yet, in conditions where market revenue plunged, costs of production and the cost-revenue gap increased. Average MY 1999-2002 US subsidies were six times greater than the period MY 1994-96, and US world market share increased to between 38 and 41.6 per cent in MY 2001-2002. These record high levels of world market share were purchased with large increases in both the quantity and level of guaranteed subsidies in MY 2001-2003 – huge marketing loan payments as well as increases in revenue support of 10 cents a pound resulting from the 2002 FSRI Act.²⁵¹ Thus, even though the period MY 1994-1996 was still heavily influenced by the revenue guarantees provided by the numerous US upland cotton subsidy programmes, this period could be a representative period for the Panel to examine for the purposes of making its "inequitable" share of world export trade findings.

²⁴⁶ Exhibit Bra-4 ("Fact Sheet: Upland Cotton", USDA, January 2003, p. 4-5).

²⁴⁷ Exhibit Bra-302 (Revised and Extended Data on Article 6.3(d) claim).

²⁴⁸ See Brazil's 9 September Further Submission, para. 110, note 145 and Figure 2.

²⁴⁹ Exhibit Bra-302 (Revised and Extended Data on Article 6.3(d) claim).

²⁵⁰ Exhibit Bra-302 (Revised and Extended Data on Article 6.3(d) claim).

²⁵¹ Brazil's 9 September Further Submission, para. 309.

184. Why does Brazil believe that an "equitable share" is one which factors out all subsidies? To the extent that domestic support and export subsidies are permitted by the *Agreement on Agriculture*, why should they not be accepted as being normal conditions in analyzing an equitable market share? (See Brazil's further submission, paras 288-289) BRA

Brazil's Answer:

189. Brazil believes, for the reasons articulated by the United States in the *EEC - Wheat Flour* dispute quoted in Brazil's Answer to Question 183, that the appropriate representative period for evaluating the *inequitable* share of share of world export trade is one in which no (or at most very few) trade-distorting subsidies were provided. Selecting an *earlier* representative period where the market share is not tainted with subsidies allows an assessment of whether a *later* market share is tainted by subsidies. As the United States argued well in *EEC - Wheat Flour*, the *inequitable* nature of a world market share can best be judged in comparison to what an *equitable*, *i.e.*, non-heavily subsidized world market share would be. This is consistent with Brazil's arguments in paragraphs 288-289 of its 9 September Further Submission that a non-subsidized world market share of 17 per cent is, by definition, an *equitable* share for the purpose of Article XVI:3. By contrast, a heavily subsidized and subsidy-increased world market share of 41.6 per cent in MY 2002 is *inequitable*.²⁵²

190. With respect to the second question, Brazil notes that although agricultural domestic and – to a certain extent - export subsidies are not prohibited, GATT Article XVI places clear limits to such subsidization. Section A determines, for example, that subsidies must be notified when they operate "directly or indirectly to increase exports of any product from, to reduce imports of any product into, its territory". More specifically, it established that the subsidizing Member must avoid causing serious prejudice to the interest of other Members. Therefore, even purely domestic subsidies should only be granted in a manner that does not affect the equilibrium of world trade that would be achieved in their absence.

191. The GATT Article XVI obligations – especially those of the second sentence of paragraph 3 – are primarily focused on the effects of subsidies that operate to increase exports. Paragraph 2 places particular emphasis on the fact that such subsidies "may cause undue disturbance" to the "normal commercial interests" of other Members. Large subsidies stimulating exports cannot be understood not to cause "undue disturbance" that affect the "normal commercial interest" of other Members. Otherwise, GATT Article XVI:3 would be stripped of any meaning. If, the starting point to an analysis of an equitable share grandfathers subsidies that were being previously granted, such analysis would start from an inequitable situation of equilibrium.

192. The term "equitable" is defined as something that is "characterized by equity or fairness; fair, just."²⁵³ "Equitable" does not relate to something that is "legal" or "permitted." Something that is permitted may well be not equitable. The fact that certain subsidies are "permitted" does not grandfather their effects and transforms them into "normal conditions in analyzing an equitable market share," as put by the Panel in this question. The text of GATT Article XVI:3 requires that the test of "equitable" market share be primarily and intrinsically linked with the concept of fairness. Therefore, an "equitable" analysis of a fair equilibrium of market shares cannot be one that starts by accepting as legitimate – or as "normal conditions" – the effects of widespread and expensive subsidies that only a few Members can afford, to the expense of developing countries.

193. Brazil does not believe that subsidies representing 95 per cent of the value of a widely-traded commodity product like upland cotton can ever be considered to have been provided under "normal conditions". Nor can a dramatic increase in absolute levels of subsidies coupled with the increase in

²⁵² See Brazil's 9 September Further Submission, para. 288.

²⁵³ The New Shorter Oxford English Dictionary, 1993 edition, p. 843.

the subsidization rate (and in absolute subsidy payments) during the period MY 1999-2002 over a previous representative period be considered to be “normal conditions”. Further, when a more than doubling of world market share by a WTO Member coincides with record low world prices, record *gaps* between total costs and market revenue and record amounts of that Member’s subsidies, the subsidies cannot be considered to have been provided in “normal conditions”.

185. Please respond to the following questions concerning the relationship between Article XVI:3 of the GATT 1994, the disciplines on export subsidies and domestic support in the Agreement on Agriculture and the disciplines on prohibited export subsidies and actionable subsidies in Articles 3, 5(c) and 6.3(d) of the SCM Agreement. BRA, US

(a) Are agricultural domestic support programmes challengeable under Article XVI:3 of the GATT 1994? How, if at all, is the title of Section B of Article XVI ("Additional provisions on export subsidies" (emphasis added)) relevant? How, if at all, are Articles 13 and 21.1, or any other provisions of the Agreement on Agriculture, relevant?

Brazil’s Answer:

194. With respect to the first question, the answer is that any domestic support programme that grants “directly or indirectly” *“any form of subsidy which operates to increase the export of any primary product”* is covered by the second sentence of Article XVI:3. All of the domestic support subsidies challenged by Brazil in this case operate to increase US exports. Professor Sumner found that each of the challenged US subsidies he examined had the effect of increasing US exports.²⁵⁴

195. Because Article XVI, including Article XVI:3, deals with serious prejudice to the interests of another Member, the direct context for interpreting its provisions is found in Article 5 of the SCM Agreement. Article 5 makes no distinction between subsidies contingent upon export and domestic support subsidies. It provides that “[n]o Member should cause, *through the use of any subsidy referred to in paragraphs 1 and 2 of Article 1*, adverse effects to the interests of other Members”. Articles 1 and 2 of the SCM Agreement in turn make no distinction between export and domestic support subsidies.

196. The United States argues that the only subsidies governed by Article XVI:3 are export subsidies.²⁵⁵ This argument misreads Article XVI:3. Although the first sentence of Article XVI:3 refers to “subsidies *on* the export of primary products,” the second sentence provides:

“If, however, a contracting party grants directly or indirectly any form of subsidy which operates to increase the export of any primary product from its territory . . .”

The word “however” is important, as it signifies that the second sentence contradicts the first and does not follow from it. Similarly, the use of the phrase “on the export of primary products” in the first sentence of Article XVI:3 is quite different from the phrase “which operates to increase the export of” in the second sentence of Article XVI:3. The notion of “on the export” is analogous to the export contingency set out in Article 3.1(a) of the SCM Agreement. However, the phrase “which operates to increase the export of” does not contain an export contingency requirement. Rather, it focuses on *effects* – whether the subsidies have the effect of increasing exports. Thus, read in light of the SCM Agreement, the second sentence of Article XVI:3 encompasses a notion of export-related subsidies that is far broader than subsidies that are “contingent upon export performance;” it includes as “export subsidies” those that operate to increase exports.

²⁵⁴ Brazil’s 9 September Further Submission, Annex I, Tables 5a -5g.

²⁵⁵ US 7 October Oral Statement, para. 61.

197. Indeed, the reading of the second sentence of Article XVI:3 as meaning “subsidies contingent upon the export of products” would render Article XVI:3 a nullity. This is because under the US interpretation, any form of subsidy covered by the second sentence of Article XVI:3 would already be deemed prohibited as an export subsidy under Article 3.1(a). Given Article 13 of the Agreement on Agriculture, GATT Article XVI:3 is clearly intended to continue to provide rights and obligations for Members. Further, Article XVI is not a prohibited subsidy provision – it is an *actionable* subsidy provision. The subsidies and the provisions of Article XVI that are not superceded by the provisions of the SCM Agreement or the Agreement on Agriculture²⁵⁶ must be read consistent with the *actionable* subsidy provisions of Article 5 of the SCM Agreement. Article 5 makes no distinction between subsidies that are contingent upon export and those that are not.

198. With respect to the Panel’s second question, the title of Section B is not determinative. In light of the use of the phrase “any form of subsidy” in the second sentence of Article XVI:3, the title of Section B is properly read as encompassing any subsidies that have any effect on a Member’s exports – whether they be “export subsidies” contingent upon export or whether they are “export subsidies” having the effect of increasing exports. Finally, Brazil notes that the US argument that places primary reliance on the title of Section B to interpret the second sentence of Article XVI: 3 is also questionable given the fact that Article XVI:5 is also covered by the title of Section B – and it deals with all types of subsidies covered by Article XVI.

199. With respect to the Panel’s reference to Article 21 of the Agreement on Agriculture, Brazil does not believe that it is particularly relevant. As the Appellate Body noted in the *EC – Bananas* case, Article 21 of the Agreement on Agriculture provides that the provisions of GATT 1994 and the other multilateral trade agreements on trade in goods “shall apply subject to the provisions of this Agreement”.²⁵⁷ The drafters of the WTO Agreement did not intend agricultural trade to be a GATT-free zone – quite the opposite. They simply provided transitional provisions in Article 13 of the Agreement on Agriculture to moderate the application of some GATT provisions, strictly on a temporary basis.²⁵⁸

200. Article 13 of the Agreement on Agriculture is not that relevant in providing guidance regarding whether domestic support measures are included within the meaning of “any type of subsidy” under Article XVI:3, second sentence. Article 13(b)(ii) exempts non-green box domestic support only from actions based on paragraph 1 of GATT Article XVI, and does not directly exempt Article XVI:3. However, Article XVI:1 and 3 must be read together in order to assert a claim of serious prejudice.²⁵⁹

201. Article 13(c)(ii) of the Agreement on Agriculture provides that during the “implementation period”, export subsidies that conform fully to Part V, as reflected in a Member's Schedule, are exempt from “actions” based on Article XVI. By implication, such export subsidies *are* subject to actions under Article XVI after the expiry of the peace clause and will be subject to such actions as of the time that the Panel issues its ruling. The same applies for green box domestic support under Article 13(a)(ii). Those subsidies are also exempt from actions under GATT Article XVI, including Article XVI:3. But these subsidies can be challenged under Article XVI:3 following the termination of the peace clause.

(b) Are the requirements of Article XVI:3 of the GATT 1994 reflected in, developed by or subsumed by the requirements in Article 6.3(d) of the SCM Agreement, or in any other

²⁵⁶ See *US- FSC*, WT/DS108/AB/R, para 117 quoted in Question 185(a).

²⁵⁷ Appellate Body Report, *EC – Bananas*, WT/DS27/AB/R, para. 155.

²⁵⁸ Appellate Body Report, *EC – Bananas*, WT/DS27/AB/R, para. 155.

²⁵⁹ Brazil’s 7 October Oral Statement, para. 59 (arguing that Articles XVI:1 and 3 are directly linked).

provisions of the covered agreements? Of what relevance, if any, is the Appellate Body Report in *US-FSC*, para. 117²⁶⁰ here?

Brazil's Answer:

202. Brazil agrees that Article 6.3(d) reflects one of the situations that would also fall under GATT Article XVI:3. An increase in the world market share compared to the previous three-year average through the effects of subsidies would be consistent with a finding of an inequitable share of world trade under GATT Article XVI:3. However, an increase over the previous three-year average is not a necessary prerequisite for a finding of a violation of GATT Article XVI:3. For example, a Member's share of world export trade may be inequitable even if that share has not increased over the average of the past three years. Similarly, a Member's increase in exports may be inequitable even if an increase in exports has not followed a consistent trend, as required under Article 6.3(d).

203. GATT Article XVI:3 is concerned with whether a particular level of a Members' share of world export trade is equitable, whereas Article 6.3(d) of the SCM Agreement only addresses an *increase* in the share. Article 6.3(d) creates a presumption that an increase in a Member's world market share over its previous three-year average that follows a consistent trend over a period when subsidies have been granted nullifies and impairs other Member's rights. No such presumption exists for Article XVI:3 – the nullification and impairment must be demonstrated by showing that the share

²⁶⁰ WT/DS108/AB/R, para 117:

"... the provisions of the *SCM Agreement* do not provide explicit assistance as to the relationship between the export subsidy provisions of the *SCM Agreement* and Article XVI:4 of the GATT 1994. In the absence of any such specific textual guidance, we must determine the relationship between Articles 1.1(a)(1) and 3.1(a) of the *SCM Agreement* and Article XVI:4 of the GATT 1994 on the basis of the texts of the relevant provisions as a whole. It is clear from even a cursory examination of Article XVI:4 of the GATT 1994 that it differs very substantially from the subsidy provisions of the *SCM Agreement*, and, in particular, from the export subsidy provisions of both the *SCM Agreement* and the *Agreement on Agriculture*. First of all, the *SCM Agreement* contains an express definition of the term "subsidy" which is not contained in Article XVI:4. In fact, as we have observed previously, the *SCM Agreement* contains a broad package of new export subsidy disciplines that "go well beyond merely applying and interpreting Articles VI, XVI and XXIII of the GATT 1947". Next, Article XVI:4 prohibits export subsidies only when they result in the export sale of a product at a price lower than the "comparable price charged for the like product to buyers in the domestic market." In contrast, the *SCM Agreement* establishes a much broader prohibition against *any* subsidy which is "contingent upon export performance". To say the least, the rule contained in Article 3.1(a) of the *SCM Agreement* that all subsidies which are "contingent upon export performance" are prohibited is significantly different from a rule that prohibits only those subsidies which result in a lower price for the exported product than the comparable price for that product when sold in the domestic market. Thus, whether or not a measure is an export subsidy under Article XVI:4 of the GATT 1947 provides no guidance in determining whether that measure is a prohibited export subsidy under Article 3.1(a) of the *SCM Agreement*. Also, and significantly, Article XVI:4 of the GATT 1994 does not apply to "primary products", which include agricultural products. Unquestionably, the explicit export subsidy disciplines, relating to agricultural products, contained in Articles 3, 8, 9 and 10 of the *Agreement on Agriculture* must clearly take precedence over the *exemption* of primary products from export subsidy disciplines in Article XVI:4 of the GATT 1994."

of world export trade is *inequitable*. While a particular situation may – as in this dispute – fall under both provisions, the focus and proof required for both provisions can be different.

204. Thus, Article 6.3(d) of the SCM Agreement subjects a specific subset of the situations covered by GATT Article XVI:3 to the remedy provided in Article 7.8 of the SCM Agreement. But it does not cover *all* of the situations covered by GATT Article XVI:3. This marks the crucial distinction between the provisions on export subsidies in the SCM Agreement that “take precedence” over those in GATT²⁶¹ and the provisions on actionable subsidies in both agreements that are complementary.

205. With respect to the Appellate Body’s holding in paragraph 117 of *US – FSC*, the provisions on export subsidies in Articles 3 and 4 of the SCM Agreement represent the results of years of negotiations that have pushed the level of obligation in this area well beyond Article XVI:4. The conclusion that the Appellate Body drew in that instance was that “whether or not a measure is an export subsidy under Article XVI:4 of the GATT 1947 provides no guidance in determining whether that measure is a prohibited export subsidy under Article 3.1(a) of the SCM Agreement.” Brazil agrees that the provisions of Article XVI:2-4 that deal with subsidies contingent upon export performance are superseded by the respective export subsidy provision contained in the Agreement on Agriculture and in the SCM Agreement.

206. However, as Brazil has argued in response to Question 185(a), the second sentence of GATT Article XVI:3 is not a provision limited to subsidies contingent upon export performance. Rather, its disciplines apply to *any* form of subsidy that operates to increase the exports of a Member. Thus, it is not superseded by the export subsidy provisions of the Agreement on Agriculture and the SCM Agreement. Rather, it provides rights and obligations concerning any form of a subsidy independent of the right and obligations set forth in Article 3 of the SCM Agreement.²⁶²

(c) Of what relevance, if any, is the fact that the definition of "subsidy" in Article 1 of the SCM Agreement and the prohibition on subsidies contingent upon export in Article 3.1(a) were introduced in the Uruguay Round, but did not exist at the time that the GATT 1947 was negotiated?

Brazil’s Answer:

207. The short answer is “not at all.” What is important for the Panel to consider is the entire package of Uruguay Round agreements, including the GATT 1994 and the contemporaneous SCM Agreement, not what was in GATT 1947.

208. Every agreement attached to the WTO Agreement is contemporaneous with every other attached agreement. The GATT 1947 no longer binds WTO Members; what is binding is the GATT 1994. The SCM Agreement and the GATT 1994 must be read together, and each provides “context” for interpreting the other, in the sense of Article 31(2) of the Vienna Convention on the Law of Treaties. As the Appellate Body noted in *Argentina – Footwear*²⁶³, and as is now well established, the WTO Agreement is a single undertaking. All WTO obligations are, therefore, generally cumulative, and Members must comply with all of them simultaneously: “It is important to understand that the WTO Agreement is *one* treaty.”²⁶⁴ Thus, in as far as GATT Article XIX and the Agreement on Safeguards apply cumulatively, GATT Article XVI and the SCM Agreement apply cumulatively.

²⁶¹ Appellate Body Report, *US – FSC*, WT/DS108/AB/R, para. 117.

²⁶² See GATT Panel Report, *EC – Sugar Exports (II)*, para. V.(g).

²⁶³ Appellate Body Report, *Argentina – Footwear Safeguards*, WT/DS121/AB/R, paras. 82-84.

²⁶⁴ Appellate Body Report, *Korea – Dairy Safeguards*, WT/DS98/AB/R, para. 74-75; quotation from para. 75 (emphasis added).

Brazil refers the Panel to its Answer to Question 185(a) for a further discussion of the issues relevant to Question 185(c).

N. CLARIFICATIONS

189. Please indicate whether the correct figure in paragraph 37 of Brazil's 7 October oral statement is 38.1 per cent or 38.3 per cent? BRA

Brazil's Answer:

209. Brazil confirms that the correct figure in paragraph 37 of Brazil's 7 October Oral Statement is 38.3 per cent, *i.e.*, that the US world market share in MY 2001 was 38.3 per cent.²⁶⁵

190. Please confirm that the figure "17.5" in paragraph 43 of Brazil's 7 October oral statement, is "percentage point". BRA

Brazil's Answer:

210. Brazil confirms that the figure "17.5" in paragraph 43 of Brazil's 7 October Oral Statement refers to an increase by 17.5 percentage points in the world market share. Brazil further notes that – as explained in note 468 to Figure 26 of its 9 September Further Submission – the world market share refers to the world market share in the international cotton market, including the upland cotton and extra-long staple cotton market, as data on upland cotton only is not available to Brazil. However, given the small size of the extra-long staple market as compared to the upland cotton market, this only minimally distorts the data.²⁶⁶

191. Could Brazil clarify its statement in para. 12 of its 9 September further submission: "Alternatively crop insurance is not specific because the 2000 ARP Act denies benefits to commodities representing more than half of the value of US agriculture. Further US crops represent only 0.8 per cent of total US GDP." (emphasis added) BRA

Brazil's Answer:

211. Brazil thanks the Panel for bringing to its attention the error in paragraph 12 of its 9 September Further Submission. As clarified in paragraphs 67-69 of the same submission, Brazil meant to state that "[a]lternatively, crop insurance *is specific* because the 2000 ARP Act denies benefits to commodities representing more than half of the value of US agriculture" (emphasis added).

²⁶⁵ Exhibit Bra -206 (Data on Article 6.3(d) claim).

²⁶⁶ Compare Exhibit Bra -208 ("Cotton: World Statistics," ICAC, September 2003, p. 2-7).

ANNEX I-6

ANSWERS OF THE UNITED STATES TO QUESTIONS FROM THE PANEL TO THE PARTIES FOLLOWING THE SECOND SESSION OF THE FIRST SUBSTANTIVE PANEL MEETING

27 October 2003

A. REQUEST FOR PRELIMINARY RULINGS

122. Does Brazil allege that cottonseed payments, interest subsidies and storage payments are included in the subsidies that cause serious prejudice? Do they appear in the economic calculations? BRA

123. Does Brazil's request for the establishment of the Panel name the statute authorizing cottonseed payments for the 1999 crop? BRA

B. EXEMPTION FROM ACTIONS

124. According to its revised timetable, the Panel will issue its report to the parties after the end of the 2003 calendar year. Does this have any impact on "exempt[ion] from actions" under Article 13(b)(ii) and 13(c)(ii) of the Agreement on Agriculture? BRA, US

1. The scheduled issuance of the Panel's report after the end of the 2003 calendar year has no impact on the applicability of Article 13(a)(ii), (b)(ii) and (c)(ii) of the Agreement on Agriculture to the US measures in this dispute. There is no question, and Brazil has not contested, that Article 13 was in effect at the time of the Panel's establishment, and the Panel's terms of reference set on that date are to examine the matter raised in Brazil's panel request in light of the covered agreements, which include the Agreement on Agriculture.

2. As a separate matter not presented by this dispute, the United States notes that the commitments of the United States with respect to cotton are specified by *marketing* year, not calendar year. Therefore, the end of the 2003 calendar year would in any case not be relevant to the question of when the provisions of Article 13 cease to have effect with respect to US support measures for upland cotton.¹

C. IDENTIFICATION OF THE SUBSIDIZED PRODUCT

125.

(1) In view of requirements in the FAIR Act of 1996 and the FSRI Act of 2002 that contract acreage remain in agricultural or conservation uses and which impose penalties if the producer grows fruits or vegetables, how likely is it that the producer with upland cotton base acreage will not use his or her land to produce programme crops or covered commodities? US

¹ See Agreement on Agriculture Article 1(i) ("'[Y]ear' in paragraph (f) above and in relation to the specific commitments of a Member refers to the calendar, financial or marketing year specified in the Schedule relating to that Member.")

3. With respect to contract acreage on a farm, the 2002 Act generally allows any commodity or crop to be planted on base acres on a farm for which direct payments are made, with limitations for certain commodities (fruits, vegetables (other than lentils, mung beans, and dry peas), and wild rice). With some exceptions, planting of those limited commodities on base acres is prohibited and could lead to reduced or eliminated direct payments.² Otherwise, a producer (or landowner) is permitted to make any other use of the land so long as the land on the farm in a quantity equal to base acreage is used for an agricultural or conserving use.³ Thus, the direct payment recipient has the flexibility to plant and harvest any other commodity or crop on the land representing their upland cotton base acreage; indeed, direct payment recipients may plant nothing at all and still receive payment. (We note that the foregoing description of the "planting flexibility" under the 2002 Act is relevant only to base acres on a farm for which direct payments are made; other acres on the farm need not comply with any of the contract requirements set out in Sections 1105 and 1106 of the 2002 Act.)

4. The data demonstrate that planting and harvesting decisions by US producers result in US upland cotton area varying significantly. In marketing year 2003, for example, US farmers planted 13,748,000 acres, a decline of 11.3 per cent from the recent high reached in marketing year 2001.⁴ As indicated in the US closing statement at the second session of the first panel meeting, US harvested acreage largely increases and decreases in line with the rest of the world.⁵ In marketing year 2001, US area harvested increased by almost the exact same percentage as did the rest of the world. In marketing year 2002, the per cent decline in harvested acreage in the United States was *greater* than that observed in the rest of the world. Thus, regardless of whether US farmers who plant upland cotton may also be holders of upland cotton base acres, and contrary to Brazil's assertions, US farmers respond to market signals by planting or harvesting upland cotton much as producers in the rest of the world do.

(2) Brazil has submitted that "The record suggests that historic producers are current producers." It points to factors including the specialization of upland cotton producers, the need to recoup expensive investments in cotton-specific equipment, and the geographic focus and climatic requirements of upland cotton production in the "cotton belt". (Brazil's rebuttal submission, footnote 98, on page 24)

(a) Regarding the specialization of upland cotton producers and the geographic focus of upland cotton production, how does Brazil take account of the fact that cotton is produced in 17 of the 50 states of the United States and that average cotton area is approximately 38% of a cotton farm's acres? (This information is taken from the US's response to question 67bis, footnote 35). BRA

(b) Regarding the geographic focus of upland cotton production, how many other crops can upland cotton producers viably grow in the cotton belt, other than fruits and vegetables? US

5. Based on planted acreage data as reported by National Agricultural Statistics Service⁶, US upland cotton is produced in several diverse regions across the Cottonbelt, generally known as the Southeast, Delta, Southwest, and West regions. Across the regions (as well as within a given region), producers are faced with differing physical growing environments as well as economic factors that help determine the viability of upland cotton or some other alternative crop in any given year. Over

² See US Answer to Question 26 from the Panel, para. 56.

³ 2002 Act, § 1105(a)(1)(D) (Exhibit US-1).

⁴ US Department of Agriculture, National Agricultural Statistics Service, *Acreage*. Cr Pr 2-5 (6-03). June 30, 2003. Available at: <http://usda.mannlib.cornell.edu/reports/nassr/field/pcp-bba/acrg0603.pdf>

⁵ See US Closing Statement at the Second Session of the First Panel Meeting, paras. 5-6; Exhibit US-63.

⁶ See Exhibit Q125(2)(b).

the last several years, producers have reduced plantings of upland cotton and increased plantings to alternatives. A list of the full range of alternative crops that are viable in these areas would be extensive. Below we present a regional breakdown of some principal alternative crops to upland cotton as well as historical plantings since 1996 of these crops compared with upland cotton.

6. Upland cotton producers in the Southeast region (Alabama, Florida, Georgia, North Carolina, South Carolina, and Virginia) have corn and soybeans as principal alternative crops. Peanuts are also an alternative, though mainly in Georgia. Between 1996 and 2003, area planted to upland cotton, corn, and soybeans in the Southeast averaged about 8.6 million acres, ranging from 8.2 to 9.1 million acres. During this same period, upland cotton area ranged from 3.0 to 3.6 million acres. Since 2001, upland cotton has been reduced in favour of corn and soybeans in this region.

7. Upland producers in the Delta region (Arkansas, Louisiana, Mississippi, Missouri, and Tennessee) also have corn and soybeans as an alternative and, to a lesser extent, rice in some areas. Between 1996 and 2003, area planted to these 4 crops averaged 22.9 million acres, ranging from 22.2 to 23.8 million. At the same time, upland cotton area ranged from 3.2 to 4.6 million acres. Like the Southeast region, the Delta area planted to upland has declined since 2001 in favour of corn and soybeans.

8. The Southwest region (Texas, Oklahoma, and Kansas) has the most diverse growing environment of the 4 regions. In the northern part of the region – where most of upland cotton is grown – principal alternatives to upland cotton may include wheat and sorghum. In the southern part, however, corn, soybeans, and sorghum are generally an alternative to upland cotton. The Southwest region planted an average of 26.3 million acres to these 5 crops between 1996 and 2003.⁷ Area ranged from 24.5 to 27.9 million acres during this period. Meanwhile, upland cotton area ranged from 5.7 to 6.7 million acres. Since 2000, upland area in the Southwest has fallen in favour of sorghum, wheat, and corn.

9. In the West region (California, Arizona, and New Mexico), upland producers have a variety of alternatives, including corn, extra-long staple (ELS) cotton, alfalfa, and wheat. Between 1996 and 2003, area planted to these 5 crops averaged 4.3 million acres in the region, ranging from 4.0 to 4.6 million. At the same time, upland cotton area has ranged from 0.7 to 1.4 million acres. The last several years, however, have seen upland area decline in favour of one or more of the alternative crops.

(c) **Regarding the high cost of upland cotton production, can Brazil show that farms who planted upland cotton could only have covered their costs by receiving upland cotton, rice or peanut payments in every year from 1999 through 2002? BRA**

(d) **Regarding the need to recoup investments in cotton-specific equipment, is it important to planting decisions that upland cotton producers cannot run any other crop through their cotton-pickers? How does this affect the likelihood that they will grow other crops? US**

10. **The National Agricultural Statistics Service (NASS) reported that in 2002, farmers paid an average of \$225,000 for a cotton picker.⁸** Farmers may respond to machinery costs through the contracting-out of harvesting operations and rental or leasing of cotton-picking machinery.

⁷To be conservative, we have excluded Kansas wheat and sorghum acreage from the totals presented due to the state's large production of these crops and relatively small production of cotton.

⁸ US Department of Agriculture, National Agricultural Statistics Service, *Agricultural Prices 2002 Summary*. Pr 1-3 (03)a July 2003. Available at: <http://usda.mannlib.cornell.edu/reports/nassr/price/zap-bb/agpran03.pdf>

11. In the short run, investment costs may slow acreage adjustments to market prices. This does not mean, however, that cotton producers do not respond to changes in market prices. Research by Lin et al. suggest that cotton producers may, in fact, be more responsive to own price changes (that is, the response of cotton acreage to changes in cotton prices as opposed to changes in prices of competing crops) **than other competing crops** are.⁹ In the long run, fixed assets like cotton pickers are less of a constraint to entry, and thus one would expect the acreage response to changes in price to be larger.

Acreage own-price elasticity for major field crops

Crop	National acreage price elasticity
Wheat	0.34
Corn	0.293
Sorghum	0.55
Barley	0.282
Oats	0.442
Soybeans	0.269
Cotton	0.466

Source: Lin *et al.*, Appendix table 21 (Exhibit US-64).

(3) In calculating the amount of PFC, MLA, direct and counter-cyclical payments that went on upland cotton, Brazil made an adjustment for the ratio of current acreage to base acreage (see its answer to question 67, footnotes 2, 3, 4 and 5). Is this an appropriate adjustment for the particular factors referred to above? Why or why not? BRA, US

12. Brazil's adjustment is not appropriate. It does not explicitly take into account any of the factors referred to above. Instead, Brazil's belated adjustment is simply based on the assumption that all of the planted cotton acreage was by producers who had cotton base acreage exactly equal to their planted acreage. This assumption is inaccurate and causes Brazil's figures to be in error. For some producers, cotton planted acres exceed their historical base, and some cotton acres are planted by producers who have no cotton base. As noted in the US further submission, important changes such as lowered costs from pest eradication and adoption of biotechnology have lowered costs and brought new areas and farmers into cotton production. Brazil's adjustment takes no account of these changes.

13. More fundamentally, the relevant point is that any producers who have upland cotton base will receive direct and counter-cyclical payments regardless of whether they plant upland cotton. Thus, the decision to plant upland cotton will be based on expected economic returns of cotton and competing crops – not the level of direct and counter-cyclical payments that are decoupled from the decision to produce upland cotton. And the fact that these are decoupled payments means that the amount of the payment could not in any event be allocated only to cotton production.

(4) Dr. Glauber has alleged that there are statistical problems in comparing planted acres to programme acres because of abandonment of crops and also because planted acres are only survey estimates, not reported figures (See Exhibit US-24, the first full paragraph in P2). Would it be more appropriate to divide harvested acreage by base acreage? What margin of error is there between the survey estimates and reported figures? BRA, US

14. Exhibit US-24 outlines the statistical problems associated with dividing complying base acres by planted acres. The discussion addressed complying base acres under the Acreage Reduction Programme of 1990 Farm Bill and did not address programme payment acres as defined under the

⁹ Lin, W., *et al.* *Supply Response Under the 1996 Farm Act and Implications for the US Field Crops Sector*. US Department of Agriculture, Economic Research Service, Technical Bulletin No. 1888, Appendix table 21 (Exhibit US-64).

1996 Farm Bill. Dividing harvested acreage by base acreage could potentially overstate the difference if there is significant acreage abandonment after producers reported their payment acres to the Farm Service Agency. Also, there remains a problem with the comparison since harvested acres are survey-based while base acres are reported numbers.

15. In the June *Acreage* report, the National Agricultural Statistics Service reports reliability estimates for selected crops. **The reliability of acreage estimates is computed by expressing the deviations between the planted acreage estimates and the final estimates as a per cent of the final estimates and averaging the squared percentage deviations for the 1983-2002 twenty-year period; the square root of this average becomes statistically the "Root Mean Square Error."** Probability statements can be made concerning expected differences in the current estimates relative to the final estimates assuming that factors affecting this year's estimate are not different from those influencing the past 20 years. For example, the "Root Mean Square Error" for the upland cotton planted estimate is 2.4 per cent. This means that chances are 2 out of 3 that the current cotton acreage will not be above or below the final estimate by more than 2.4 per cent. NASS reports that the 90 per cent confidence interval for the upland cotton estimate is 4.1 per cent. This means that chances are 9 out of 10 (90 per cent confidence level) that the difference will not exceed 4.1 per cent.¹⁰

(5) Do the acreage reports under section 1105(c) of the FSRI Act of 2002 indicate or assist in determining the number or proportion of acres of upland cotton planted on upland cotton base acres? Was there an acreage reporting requirement for upland cotton during MY1996 through 2002? BRA, US

16. The acreage reports filed under Section 1105(c) of the 2002 Act by farms receiving direct and counter-cyclical payments indicate what crops are planted on a farm. A farm is an administrative construct that consists of tracts of land that are operated as one unit. The farm may be operated by more than one producer, and a producer may produce crops on more than one farm. The acreage report does not indicate the quantity of base acres on the farm. Because the acreage reports are filed after the planting season but before the harvest, the reports do not contain information on the quantity of production on each farm.

17. Based on a very preliminary review of a sampling of marketing year 2002 acreage reports, the United States estimates that roughly 53 per cent of farms that were eligible for direct and counter-cyclical payments for upland cotton base acreage also planted at least one acre of upland cotton in 2002. That is, approximately 47 per cent of farms receiving direct and counter-cyclical payments in 2002 for upland cotton base acreage planted no upland cotton at all.

18. Over the period 1996 through 2002, there was no statutory requirement for acreage reports by recipients of decoupled payments or marketing loan payments. By regulation, producers who signed up for disaster assistance or who received marketing loan benefits (including loan deficiency payments) were asked to file planting acreage reports. Reports for producers receiving disaster assistance were to cover all acreage on the farm while reports for producers receiving marketing loan benefits were to cover only acreage for the crop receiving benefits. As a result, acreage reports over the period of the 1996 Act are incomplete.

(6) Please prepare a chart showing upland cotton base acreage, planted acreage and harvested acreage for MY1996 through 2002. Does the planted acreage fluctuate within a broad band? If not, does this indicate any stability in decisions to plant the same acres to upland cotton? BRA, US

¹⁰ US Department of Agriculture. National Agricultural Statistics Service. *Acreage*. CrPr 2-5 (6-03). 30 June 2003. Pp 38-39.

19. The following chart shows upland cotton base acreage, planted acreage and harvested acreage for marketing years 1996 through 2002:

US upland cotton area (thousand acres)

Crop year	Base acreage 1/	Planted acreage 2/	Harvested acreage 2/
1996	16128	14395	12632
1997	16213	13648	13157
1998	16412	13064	10449
1999	16377	14584	13138
2000	16268	15347	12884
2001	16239	15499	13560
2002	16217 (est.)	13714	12184

1/ US Department of Agriculture, Farm Service Agency

2/ US Department of Agriculture, National Agricultural Statistics Service, selected Acreage reports

20. Over the period 1996-2002, US upland cotton planted acres ranged considerably, from 13,064,000 acres to 15,499,000 acres. Year-over-year, planted and harvested acreage can rise or fall significantly. For example, from marketing year 2001 to marketing year 2002, planted acreage fell by 1.785 million acres or 11.5 per cent; harvested acreage fell by 1.376 million acres or 10.1 per cent. As was pointed out in the US closing statement at the second session of the first substantive meeting of the Panel and in Exhibit US-63, year-over-year changes in US harvested cotton acreage have been similar to year-over-year changes for harvested cotton acreage outside of the United States. These data do not provide any information on whether the same or different acres are planted to upland cotton.

21. As noted above in the US answer to Question 125(5), based on a preliminary review of a sampling of marketing year 2002 acreage reports, it would appear that nearly half of farms receiving direct and counter-cyclical payments in 2002 for upland cotton base acreage planted no upland cotton at all. That so many farms that produced upland cotton during the historical base period of 1993-1995 or 1998-2001 no longer plant even a single acre of upland cotton suggests that there has been a large exit of past cotton producers and a large entry of new producers or a large expansion by other historical cotton producers.

(7) Brazil states that one third of all US farms with eligible acreage decided to update their base acreage under the direct payments and counter-cyclical payments programmes using their MY1998-2001 acreage. What is the proportion of the current base acreage for upland cotton resulting from such updating? Is the observed updating of base acreage consistent with Brazil's argument that it is only profitable to grow upland cotton on base acreage (and peanut and rice base acreage)? BRA

(8) How could one take account of upland cotton producers who receive PFC, MLA, direct and counter-cyclical payments for other covered commodity base acreage? BRA, US

22. Under Brazil's approach, one would need to take account of upland cotton producers receiving decoupled payments only for base acreage for other covered commodities. This follows from Brazil's explanation that "only the portion of upland cotton [decoupled] payments that actually benefits acres planted to upland cotton can be considered support to upland cotton".¹¹ Thus, under Brazil's approach, one would need to deduct any production (or acreage) attributable to such producers from the acreage figures Brazil has used to adjust the amount of decoupled payments on upland cotton base acreage.

¹¹ Brazil's Answer to Question 67 from the Panel, fn. 2-5.

- (9) Assuming that Brazil's payment figures were to amount to a prima facie case, please answer the following questions: US
- (a) How would the United States calculate or estimate the proportion of upland cotton producers who receive subsidy payments for upland cotton base acreage?
 - (b) Should any adjustment estimates be made for any factors besides those listed by Brazil?
 - (c) What adjustment estimate would it be appropriate to make?
 - (d) How could one take account of upland cotton producers who receive decoupled payments for other programme crop base acreage?
 - (e) Could the US specifically indicate what, in its view, are the flaws in the approach summarized in paras. 6-7 of Brazil's closing oral statement on 9 October (i.e. the use of the ration of 0.87 to adjust the amount of total upland cotton direct and CCPs for the MY to obtain the amount of subsidies received by upland cotton producers)? Can the US suggest an alternative approach that would yield reliable results in its view?

23. Putting Peace Clause and green box issues to one side, the United States believes that the issue of what payments may be attributed to upland cotton production is fundamentally part of Brazil's burden to present evidence substantiating the amount of the subsidy that it is challenging. However, the United States would note that this issue is not a matter of "the proportion of upland cotton producers who receive subsidy payments for upland cotton base acreage." Rather, the issue is, first, what is the quantity of decoupled payments received by upland cotton producers; second, how are those payments allocated across the total value of each farm's agricultural production; and third, how much and in what amount are US cotton exports subsidized by these payments.

24. Brazil has conceded that decoupled payments made with respect to upland cotton base acreage are not "tied to the production or sale" of upland cotton, by adjusting such payments by 0.87.¹² That is, Brazil recognizes that, even on its theory, at least 0.13 of these payments "can[not] be considered support to upland cotton" because at least that fraction of upland cotton base acres were not planted to upland cotton in marketing year 2002. Because these payments are not "tied to the production or sale" of upland cotton, as suggested by Annex IV of the Subsidies Agreement, they must be allocated across the total value of production of each recipient. Brazil has not denied the applicability of the allocation methodology set out in Annex IV, but neither has Brazil provided any evidence relating to the total value of production of decoupled payment recipients.¹³

25. Brazil claims that its "suggested methodology is based on the conclusion that all upland cotton producers received these payments".¹⁴ In fact, Brazil's methodology is based on the further assumptions that (1) every acre of upland cotton in marketing year 2002 was planted by a holder of upland cotton base acreage and (2) no such base acreage holder planted more upland cotton than his or her base acres.¹⁵ Brazil has provided no evidence to support these assumptions, which is no

¹² In addition to issues relating to the "adjustment," the United States disagrees with the total amount of decoupled payments paid with respect to upland cotton base acreage that Brazil calculates and uses as the base for its adjusted payment amounts. See US Answer to Additional Question 67bis from the Panel, para. 28, fn. 37, 38.

¹³ As noted in the Panel's Question 125(2)(a), average cotton area is approximately 38 per cent of a cotton farm's acres. Thus, a substantial portion of the average cotton farm's agricultural production will be derived from production of other crops.

¹⁴ Brazil's Closing Statement at the Second Session of the First Panel Meeting, para. 8.

¹⁵ Using figures for marketing year 2002 planted acreage and base acreage, Brazil claims, "Out of the 16.2 million upland cotton base acres, 2.1 million were not planted to upland cotton in MY2002." Brazil's Closing Statement at the Second Session of the First Panel Meeting, para. 6. However, given the planting and

surprise since the evidence is to the contrary. For example, the fluctuations in upland cotton planted and harvested area in recent years and the fact that one-third of all US farms with eligible acreage decided to update their base acreage using their MY1998-2001 acreage, imply substantial new entrants or new acreage that were not included in the base period figures under the 1996 Act. In fact, as noted above in the US answer to Question 125(5), based on a preliminary review of marketing year 2002 acreage reports, the United States estimates that nearly half of all farms receiving direct and counter-cyclical payments in 2002 for upland cotton base acreage planted no upland cotton at all.

26. We also note that there are substantial requirements with which a payment recipient must comply (see US answer to Question 162), such as highly erodible cropland conservation requirements and wetland conservation requirements.

D. "LIKE PRODUCT"

126. Does the US agree that the product at issue is upland cotton lint and that Brazilian upland cotton lint is "like" US upland cotton lint within the meaning of Article 6.3(c) of the SCM Agreement in that it is a separate like product that is identical or has characteristics similar to the upland cotton lint from the United States? (e.g. Brazil's further submission, para. 81) US

27. For purposes of this dispute, the United States is not arguing that all US cotton is "unlike" Brazilian cotton. There are some grades of cotton that both produce. Such grades would have similar characteristics although, as noted by Mr. Ward at the second session of the first panel meeting, Brazilian lint has been sold in the past at a substantial discount to the New York futures price. That discount has been declining over time as Brazil, a relatively new supplier internationally, works to establish a reputation for quality and reliability.

E. "SUBSIDIES"

127. The Panel notes that the US contests that export credit guarantees constitute "subsidies". The Panel recalls that the US agrees that Step 2 payments are "subsidies" and wishes to have confirmation that it is correct in understanding that the US does not disagree that the following are "subsidies" for the purposes of Article 1 of the SCM Agreement: marketing loan/loan deficiency payments, PFC, direct payments, market loss assistance and CCP payments, crop insurance payments, cottonseed payments, storage payments and interest subsidy (without prejudice to the Panel's rulings on the US requests for preliminary rulings on the latter two payments). US

28. With respect to marketing loan payments, the United States agrees that these product-specific amber box payments that are made to producers of upland cotton for the production of upland cotton are subsidies within the meaning of Article 1 of the Subsidies Agreement.

29. With respect to crop insurance payments, through which the United States pays a portion of the crop insurance premium for producers, the United States agrees that these amber box payments are subsidies within the meaning of Article 1 of the Subsidies Agreement. We note, however, that these payments are not product-specific because they are not made to upland cotton producers for the production of upland cotton. Rather, they are non-product-specific support made to "producers in general" (that is, generally). Further, these crop insurance payments are not specific within the meaning of Article 2 of the Subsidies Agreement because they are available with respect to all

base acreage numbers, the most Brazil can logically claim is that "at least 2.1 million [base acres] were not planted to upland cotton in MY2002". That is, if in 2002 new producers without base acres planted upland cotton or if some historical producers planted more than their base acres, then some portion of the 14.1 million planted acres in MY2002 were not planted "on" upland cotton base acres.

agricultural products for which policies are offered by private companies. Therefore, pursuant to Article 1.2, this “subsidy” is not subject to the provisions of Part III of the Subsidies Agreement.

30. With respect to cottonseed payments, we recall that these payments are not within the terms of reference of the Panel.¹⁶ With respect to “other payments” for upland cotton notified by the United States to the WTO – that is, storage payments and interest subsidy – the United States also recalls that these payments are not within the Panel’s terms of reference.¹⁷ Without prejudice to the US request for preliminary rulings on these three types of payments, the United States considers that these product-specific amber box payments are subsidies within the meaning of Article 1.

31. With respect to green box production flexibility contract payments under the 1996 Act and direct payments under the 2002 Act, the United States does not consider that Brazil has demonstrated what is the amount of the subsidy attributable to upland cotton producers pursuant to Article 1. Article 1 requires that a financial contribution by a government or public body or income or price support confers a benefit. The subsidies Brazil challenges are subsidies to producers, users, and/or exporters of upland cotton. However, Brazil has not identified the portion of the production flexibility contract payments that is properly attributable to upland cotton producers as opposed to other recipients of this subsidy. In fact, Brazil concedes that the entire amount of these payments does not confer a benefit on upland cotton producers by reducing the amount of production flexibility contract payments and direct payments on upland cotton base acres by the proportion 14/16. However, Brazil has provided no evidence of the amount of these decoupled payments received by producers that currently produce cotton. Nor has Brazil demonstrated how much or to what extent US cotton exports are subsidized.

32. With respect to *ad hoc* market loss assistance and counter-cyclical payments under the 2002 Act, the United States also does not consider that Brazil has demonstrated what is the amount of the subsidy attributable to upland cotton producers pursuant to Article 1. Specifically, as with production flexibility contract payments and direct payments, Brazil has not identified the portion of the subsidy that is properly attributable to producers of upland cotton as opposed to other recipients of this subsidy. Brazil has not identified the benefit to upland cotton producers conferred by these payments. Rather, Brazil merely assumes that for every upland cotton harvested acre, upland cotton producers had a corresponding upland cotton base acre. However, Brazil has provided no evidence of the amount of these decoupled payments received by producers that currently produce cotton.

F. PROHIBITED SUBSIDIES

128. Could the US respond to Brazil's assertions relating to the meaning and effect of the introductory phrase of Article 3 ("Except as provided in the Agreement on Agriculture...")? Would the meaning/effect change if Article 13 of the Agreement on Agriculture did not exist? BRA, US

33. It is not entirely clear to the United States to which assertions of Brazil the Panel refers in its question. Moreover, the United States does not believe Brazil has purported to ascribe a specific meaning to that particular phrase. Indeed, with respect to Article 3.1(b), Brazil’s arguments would effectively delete the introductory phrase in its entirety.¹⁸

G. SPECIFICITY / CROP INSURANCE

129. In the event that the Panel does not consider that the alleged prohibited subsidies fall within the provisions of Article 3 and are therefore, pursuant to Article 2.3, "deemed to be

¹⁶ See, e.g., US Further Submission, para. 8.

¹⁷ See US Further Submission, paras. 6-7.

¹⁸ See Answer of the United States to Panel Question 144, *infra*.

specific", are there any other grounds on which Brazil would rely in order to support the view that such measures are "specific" within the meaning of Article 2 of the SCM Agreement (see, for example, fn 16 of Brazil's further submission)? BRA

130. Does Brazil agree that the US insurance premium subsidy is available in respect of all agricultural products? Please cite relevant portions of the record. BRA

131. How should the concept of specificity - and, in particular, the concept of specificity to "an enterprise or industry or group of enterprises or industries" -- in Article 2 of the SCM Agreement apply to subsidies in respect of agricultural commodities? Please answer the following questions, citing the principles in Article 2 of the SCM Agreement: BRA, US

(a) is a subsidy in respect of all agricultural, but not other, products specific?

34. The United States does not regard a domestic subsidy as being specific solely because the subsidy is limited to the agricultural sector. As previously noted, this proposition is codified in the US countervailing duty regulations, at 19 C.F.R. § 351.502(d). Thus, the United States is of the view that the agricultural sector is too broad and too diverse to constitute a single "enterprise or industry or group of enterprises or industries".

(b) is a subsidy in respect of all agricultural crops (i.e. but not to other agricultural commodities, such as livestock) specific?

35. It is difficult to opine on this question in the abstract. However, this fact pattern does not apply to the US insurance premium subsidies, which are also available in respect of livestock.

(c) is a subsidy in respect of certain identified agricultural products specific?

36. It is difficult to opine on this question in the abstract. However, this fact pattern does not apply to the US insurance premium subsidies since the premium subsidy is a single subsidy programme available in respect of all products (while policies issued by private parties are in certain instances available in respect of certain identified products).

(d) is a subsidy in respect of upland cotton, but not other products, specific?

37. The United States assumes that this would require that the subsidy be limited to certain entities or the upland cotton industry and so would be specific. This fact pattern, however, does not apply to the US insurance premium subsidies since the premium subsidy is a single subsidy programme available with respect to all products (while policies issued by private parties are in certain instances available in respect of certain identified products).

(e) is a subsidy in respect of a certain proportion of the value of total US commodities (or total US agricultural commodities) specific?

38. In principle, a subsidy that is limited to a sufficiently small proportion of US commodities would be "limited", and, thus, "specific" within the meaning of Article 2.1(c). However, the Subsidies Agreement does not establish any quantitative standards for determining when a subsidy is so limited, and a proposal to establish such standards was rejected during the Uruguay Round. Therefore, the determination must be made on the basis of the facts of the particular case. This is the approach taken by the US Department of Commerce for purposes of the US countervailing duty law.

(f) is a subsidy in respect of a certain proportion of total US farmland specific?

39. This question is not presented in this dispute, but the United States would note that “land” is neither an “enterprise” nor an “industry”, and so the proportion of farmland as such would not be appear to be relevant to the analysis under Article 2 of the Subsidies Agreement. The issue also does not appear to fall within the scope of Article 2.2, which deals with regional specificity – that is, “total US farmland” does not correspond to a “designated geographical region”.

132. Please state the amount and percentage of upland cotton acreage covered by each crop insurance programme and/or policy under the ARP Act of 2000. US

40. There is one crop insurance programme, through which the United States provides premium subsidies on crop insurance policies that are offered by private insurance companies under the authority of the Federal Crop Insurance Act. There is no specific crop insurance programme or policies for cotton authorized under the Agricultural Risk Protection Act of 2000. Within this crop insurance programme, there are different plans of insurance that offer different types of coverage, such as production plans of insurance or revenue plans of insurance. All such plans of insurance are reinsured by FCIC and a premium subsidy paid by the US Government, is available. The amount and percentage of upland cotton acreage covered by each plan of insurance is shown in Exhibit US-65.

133. Concerning Brazil's arguments in its oral statement, para. 7, can the US indicate if any producers of livestock outside a pilot programme are covered by the crop insurance programme? US

41. Yes, producers of livestock outside of pilot programmes are covered by the crop insurance programme. In addition, there are policies being developed pursuant to pilot programmes in order to expand the scope of insurance products offered by private insurers to livestock producers. Thus, US crop insurance payments on premiums are made to a broad range of agricultural producers across the agricultural sector, including many livestock producers.

42. Livestock producers are eligible for several forms of “crop insurance” benefits under the provisions of the same operational statute that provides for benefits for “crops”. Under the Federal Crop Insurance Act (7 USC 1501-1524), the Federal Crop Insurance Corporation (FCIC), an entity within the US Department of Agriculture, can approve insurance products if there is “sufficient actuarial data” to justify it to producers of “agricultural commodities”.¹⁹ See 7 USC 1508(a). The Act defines “agricultural commodity” to include a lengthy list of commodities, including such non-plant commodities as “finfish” and “mollusks”. The definition also includes any “other agricultural commodity”, except stored grain (the crop that produced the grain would be eligible for coverage), as determined by the Board of Directors of FCIC.

43. Thus, FCIC has the authority to offer insurance for livestock under its regular insurance programmes. The FCIC has approved products providing income protection to producers with livestock on their farm as contemplated in the statute. In addition, with the enactment of the Agricultural Risk Protection Act of 2000 (ARPA) (Pub. Law 106-224), Congress specifically mandated that FCIC offer pilot programmes for livestock. See 7 USC 1523.

44. The Adjusted Gross Revenue (AGR) product provides protection against low revenue due to unavoidable natural disasters and market fluctuations that occur during the insurance year. Covered farm revenue consists of income from all agricultural commodities, including amounts of income from animals and animal products and aquaculture reared in a controlled environment. To be eligible to purchase an AGR policy, the producer can earn no more than 35 per cent of expected allowable income from animals and animal products. Because the amount of livestock is considered incidental,

¹⁹ See 7 US Code § 1508.

the expenditures are not counted against the funding limitations for livestock contained in 7 USC 1523 (which have never been reached).

45. The 35 per cent limit does not apply in the so-called "AGR-lite" programme, which was developed by, and originally available only in, Pennsylvania, the state that developed the policy. However, beginning with the 2004 crop year, an "AGR-lite" product will be expanded to counties in Connecticut, Delaware, Maine, Vermont, Massachusetts, New Hampshire, New Jersey and Rhode Island, and selected counties in West Virginia, New York, and Maryland, as approved by RMA. In all, the AGR-lite programme will now cover about 300 counties. That expansion of AGR-Lite was announced in an 18 August 2003, press release, available on the RMA website.

46. There are at least four kinds of products specifically for livestock available to livestock producers, and they are described at the website of the Risk Management Agency (RMA) (www.rma.usda.gov). There are two different policies that are available for swine producers. The first is Livestock Risk Protect (LRP- Swine). Originally that product was available only in Iowa. RMA recently announced that the policy may be offered to swine producers in 10 additional states: Illinois, Indiana, Kansas, Minnesota, Nebraska, Nevada, Oklahoma, Texas, Utah and Wyoming. The other policy available to swine producers is Livestock Gross Margin (LGM), which is available in Iowa. For cattle, there are two specialized policies available. Livestock producers may purchase a LRP-Feeder Cattle policy in Colorado, Iowa, Kansas, Nebraska, Nevada, Oklahoma, South Dakota, Texas, Utah, and Wyoming. Finally, there are "LRP-Fed Cattle" policies in Illinois, Iowa and Nebraska.

134. Please state the annual amount of premiums paid or contributions made by US upland cotton farmers relating to each of the crop insurance programmes and/or policies supported by the US Risk Management Agency and the Federal Crop Insurance Corporation in each year from 1992 through 2002. US

47. Please see Exhibit US-66.

135. Please state the annual amount of insurance indemnity payments made by the US government; or insurance companies participating in crop insurance programmes and/or policies under the ARP Act of 2000 to upland cotton farmers in each year from 1992 through 2002. US

48. Please see Exhibit US-67.

136. Is the US arguing that crop insurance subsidies corresponding to "over 90 per cent of insured cotton area" (US 7 October oral statement, para. 46) in MY1999 through 2002 are consistent with paragraph 8(a) of Annex 2 of the Agreement on Agriculture? Is it correct that in the past these subsidies were nonetheless notified to the Committee on Agriculture as non-product specific AMS (see, for example, G/AG/N/USA/43 in Exhibit BRA-47)? US

49. The United States has notified crop insurance payments to the Committee on Agriculture as non-product specific support. This is consistent with the US position that crop insurance subsidies are generally available subsidies to the agricultural sector as a whole.²⁰ In the US oral statement of 7 October 2003, it is pointed out that over 90 per cent of the cotton area currently under the programme is insured at coverage levels of 70 per cent or less of expected yield (or revenue). Over all commodities, almost 70 per cent of total insured area is insured at 70 per cent or less of expected yield or revenue. Thus, associated subsidies would be consistent with paragraph 8(a) of Annex 2 of the Agreement on Agriculture – that is, payments for relief from natural disasters that Members have

²⁰ US Comments on Brazil's Rebuttal Submission, paras. 34-42; US Rebuttal Submission, paras. 93-98; US Further Submission of September 30, 2003, paras. 14-15.

agreed have no or at most minimal trade-distorting effects or effects on production. The point is made to stress that such subsidies that satisfy green box criteria are likely non-production distorting, contrary to the assertions made by Brazil.

H. EXPORT CREDIT GUARANTEES

137. Please elaborate the meaning of "net losses" as is used in paragraph 70 of Brazil's 7 October oral statement. BRA

138. Please comment on Brazil's views stated in paragraph 70 of its 7 October oral statement. US

50. In specific response to Brazil's views stated in that paragraph, the United States invites the attention of the Panel to paragraphs 157-162 of the 22 August US Rebuttal Submission, the table accompanying paragraph 161 of that submission, and paragraphs 144-150 of 30 September Further Submission of the United States. Paragraph 70 of Brazil's 7 October oral statement is simply a recapitulation of arguments it had previously advanced.

51. As noted in paragraph 144 of the US Further Submission, current data for each of the cohorts for 1992, 1993, 1994, 1995, 1996, and 1999 indicates a profit.²¹ As stated in OMB Circular No. A-11: "The subsidy cost is the estimated present value of the cash flows . . . resulting from a direct loan or loan guarantee A positive net present value means that the Government is extending a subsidy to borrowers; *a negative present value means that the credit programme generates a 'profit' (excluding administrative costs) to the Government.*"²²

139. In the context of export credit guarantees, is the Panel correct in understanding that Brazil's claims of inconsistency with the Agriculture Agreement involve GSM 102, GSM 103 and SCGP, but that it limits its "serious prejudice" allegations in respect of export credit guarantee programmes to the GSM 102 programme, and does not challenge GSM 103 and SCGP in this respect? If so,

- (a) could Brazil please explain why it did so, and confirm that all the data relied upon in its further submissions (e.g. in Table 13) relate to the GSM 102 programme rather than to GSM 102, GSM 103 and SCGP (and, if the data needs to be adjusted to take account of a narrower "serious prejudice" focus, supply GSM-102-relevant data)? BRA**
- (b) for the purposes of Article 13(c)(ii) of the Agreement on Agriculture, is it necessary for the Panel to examine only GSM 102 or should the Panel's examination include also GSM 103 and SCGP? Why or why not? BRA**

140. Could Brazil explain how, if at all, it has treated export credit guarantees for the purpose of Table 1 of its further submission? BRA

141. The Panel notes the US argument, inter alia in its further submission, that the export credit guarantee programmes are "self-sustaining". Recalling that item (j) of the Illustrative List of Export Subsidies in Annex I of the SCM Agreement refers to "premium rates", could the US expand upon how it takes into account the premium rates for the export credit guarantee programmes in its analysis. US

²¹ See also US Rebuttal Submission, para. 161 (chart of Subsidy Estimates and Reestimates by Cohort); US Further Submission, fns. 82 and 96.

²² OMB Circular No. A-11, section 185.2, pp. 185-3 and 185-4 (italics added) (Exhibit Bra -116).

52. Item (j) of the Illustrative List of Export Subsidies in Annex I of the SCM Agreement is concerned with whether premium rates are inadequate to cover the long-term operating costs and losses of the programmes. **A rate is applied against a transaction amount to generate revenue to cover any costs and losses. In the context of the export credit guarantee programmes, the premium rate is applied against the volume of a particular transaction to generate revenue. The mere rate as an abstract number cannot generate revenue. Consequently, premium rates as applied to the volume of transactions is necessarily the principal source of programme revenue. In addition, recoveries – whether direct or through rescheduling – are an additional source of revenue. Revenue from all these sources are applied against its operating costs (e.g., administrative expenses) and losses from its claims experience. Alternatively, such recoveries may be viewed not as revenue but as a reduction of loss arising from claims experience. For example, a full recovery of an amount already paid as a claim yields a net loss of zero. Arithmetically, this would yield the same result as treating the recovery as revenue, offsetting the equivalent amount of prior loss.**

53. As the United States noted in footnote 81 of its 30 September Further Submission, Brazil has erroneously argued that item (j) compels consideration only of premiums on the revenue side of the ledger for purposes of covering long-term operating costs and losses. In Brazil's Comment on the US answer to Panel question 77 (para. 94), Brazil states that "item (j) limits the revenue to be used to offset operating costs and losses to 'premium rates'". To the contrary, item (j) envisions an examination of whether premium rates are inadequate to cover long-term operating costs and losses. It does not say that all other revenue must be excluded from the calculation of whether a loss has occurred. Brazil would argue that if the United States paid a claim on day 1 and recouped in full on day 2 the amount it had paid, it could not include such recovery in a determination of whether the programme satisfied item (j). Such a draconian result is economically illogical and certainly not compelled by the text. As noted above, whether the recovery is viewed as revenue or as a subtraction from loss, the net result would be the same, but it must be included in any evaluation of whether premium rates cover long-term operating costs and losses.

54. As the United States further noted in its response to Panel question 77 (11 August Answers to Panel Questions, para. 145), item (j) applies to three different types of programmes: export credits, export credit guarantees, and insurance. In the case of export credit guarantees and insurance, the provider will occasionally incur claims. To the extent such claims or defaults exceed revenue from whatever source it may be derived, the net result would be a loss arising from operations. In an accounting sense such result would constitute an 'operating loss.'

55. Revenues derived from fees paid in connection with the export credit guarantee programmes form an integral part of the estimate and re-estimate process that currently indicate profitability for each of the cohorts in 1992, 1993, 1994, 1995, 1996, and 1999.²³ The application of the rates in this regard to the analysis is properly extended to 1992, as this is the first fiscal year of applicability of government-wide accounting for federal credit programmes under the Credit Reform Act of 1990. This period also conforms with the period that Brazil recognizes as appropriate for analysis under item (j).²⁴ As a result of such profitability, the programmes are self-sustaining.

142. The US has pointed out that there are many limitations on granting export credit guarantees and that there is no requirement to issue any particular guarantee (US further

²³ See Answer of the United States to Panel Question 138, *supra*. See also US Rebuttal Submission, para. 161 (chart of subsidy estimates and reestimates by cohort); US Further Submission, fns. 82 and 96.

²⁴ See First Submission of Brazil (24 June 2003), para. 282: "[A] ten-year period . . . fulfils the criterion of being 'long-term' within the meaning of item (j)." In contrast, no such long-term analysis is possible with respect to the Supplier Credit Guarantee Programme, the regulations for which were first promulgated only on 1 July 1996, with transactions commencing during fiscal year 1997.

submission, paras 153-156). Can the Commodity Credit Corporation decline to grant an export credit guarantee even in cases where the programme conditions are met? US

56. A proper response to this question requires one to define by what is meant by “programme conditions”. The arguments of Brazil would appear to create a tautological circularity: if one assumes that none of the various discretionary programmatic and budgetary bases that would permit the Commodity Credit Corporation not to issue a particular export credit guarantee are in effect, then can the CCC decline to grant that particular guarantee? Under those circumstances the question itself dictates that the answer must be “no”. The United States submits, however, that assuming away all of the real-world bases that would permit CCC to decline issuance of a guarantee is not a proper basis for analysis.

57. The fact remains, as the United States has pointed out, that numerous bases exist for denial of a guarantee.²⁵ Brazil has argued, however, that “CCC does not enjoy the discretion to refuse to issue a guarantee to an eligible individual”.²⁶ This is simply not true. Perhaps a practical example would further illustrate the point. As the United States mentioned during the first substantive meeting of the Panel, CCC internally maintains limits on the amount of its exposure to obligations of particular foreign banks.²⁷ Although a qualified applicant might apply for an export credit guarantee for an eligible good to an eligible destination (each of those elements themselves constituting potential bases for denying an application), notwithstanding the eligibility of the applicant, good, and destination, if the foreign-bank obligor envisioned in the transaction would exceed the applicable *internally established* exposure limit if it consummated the transaction, CCC could and would deny the application for the guarantee. Thus, while it is true that the CCC does not engage in any *arbitrary* or *standard-less* denials, the point is that no exporter seeking to engage in a particular export transaction can be certain of obtaining a credit because of CCC decisions relating to the conditions for issuance of export credit guarantees.

143. Brazil agrees with National Cotton Council estimates of the effects of the GSM 102 programmes (Brazil's further submission, para. 190) but it also cites a different conclusion by Prof. Sumner (paragraph 192). Brazil cites other estimates by Prof. Sumner throughout its further submission. Does Brazil adopt Prof. Sumner's conclusions and estimates as part of its submission? BRA

I. STEP 2 PAYMENTS

144. Is the Panel correct in understanding that the US does not dispute that Step 2 (domestic) payments are contingent upon import substitution, and that it argues that such measures are permitted due to the operation of the provisions of the Agreement on Agriculture? How is that relevant to a claim under Articles 5 and 6 of the SCM Agreement? US

58. The United States acknowledges that to receive a payment under the Step 2 programme a domestic user must open a bale of domestically produced baled upland cotton. As the United States noted in its Further Submission of 30 September 2003²⁸, the introductory clause of Article 3.1 of the Subsidies Agreement, “Except as provided in the Agreement on Agriculture”, applies to both Articles 3.1(a) and 3.1(b). Brazil’s arguments would delete the application of the introductory clause to Article 3.1(b). As the exception’s applicability to Article 3.1(b) must be given meaning, the United States has noted that the Agreement on Agriculture does permit domestic content subsidies in favour

²⁵ See, e.g., US Further Submission (30 September), paras. 153-156

²⁶ Second Oral Statement of Brazil (7 October), para. 67.

²⁷ See http://www.fsa.usda.gov/cc/banks_foreign_rqts.htm

²⁸ Paras. 165-176.

of agricultural producers, albeit paid to processors, if such subsidies are provided consistently with the Member's domestic support reduction commitments.²⁹ The European Communities concur.³⁰

59. As the United States has previously indicated to the Panel³¹, the United States reports all Step 2 payments as product-specific domestic support to cotton. As the United States is entitled to the protection of the Peace Clause under Article 13(b)(ii) of the Agreement on Agriculture, the United States is exempt from action under Articles 5 and 6 of the Subsidies Agreement. By their express terms, Articles 5 and 6 do "not apply to subsidies maintained on agricultural products as provided in Article 13 of the Agreement on Agriculture".

60. The question of "import substitution" is otherwise irrelevant to Brazil's claims under Articles 5(c) and 6, which focus on the effect of the particular subsidy without regard to the origin requirements of the subsidy. In contrast, Article 3.1(b) focuses on whether a subsidy is contingent upon use of domestic over imported goods to determine whether a particular subsidy is a prohibited subsidy irrespective of its effect.

J. ACTIONABLE SUBSIDIES

145. The Panel notes that different remedies are available in respect of prohibited and actionable subsidies under Articles 4.7 and 7.8 of the SCM Agreement. If the Panel were to conclude that a subsidy was prohibited and were to make a recommendation under Article 4.7 of the SCM Agreement to withdraw the subsidy without delay, can the Panel:

- (a) also conclude that the same subsidy had resulted in adverse effects to the interests of another Member? If so, what would be the value of such a conclusion in terms of the settlement of the matter before the Panel? BRA, US**
- (b) take into account the effects of the interaction of those prohibited subsidies with other, allegedly, actionable subsidies? If so, how is this relevant to the issue of causation under Article 5 of the SCM Agreement? BRA, US**

61. As a practical matter, there may be limited value in a particular dispute from making a finding that a particular subsidy is both a prohibited subsidy and causes adverse effects. If a subsidy is prohibited, then the remedy required to be recommended under Article 4.7 is to withdraw the subsidy without delay. A finding at the same time that a subsidy causes serious prejudice, if done cumulatively with an analysis of other subsidies, would mean that it would leave unclear the question of whether the other, non-prohibited subsidies cause adverse effects. That may diminish the value (in terms of resolving the dispute) of any finding concerning those other subsidies.

62. On the other hand, if the Panel were to make a separate "adverse effects" analysis for each of the non-prohibited subsidies, there would be no reason to so analyze any prohibited subsidy. First, an adverse effects analysis of a prohibited subsidy could not affect a panel's findings with respect to each non-prohibited subsidy. Second, since under Article 4 the panel would have recommended withdrawal of the prohibited subsidy, compliance with Article 4 would also comply with a recommendation under Article 7. Therefore, having made a recommendation under Article 4 with respect to a subsidy, there would be no utility to also making a recommendation under Article 7.

²⁹ US Further Submission (September 30, 2003), para. 167; First Written Submission of the United States, paras. 146-150.

³⁰ Answers of the European Communities to Panel Question 40, paras. 72-78; First Oral Statement of the European Communities, paras. 31-37.

³¹ See, e.g., First Written Submission of the United States, para. 129; G/AG/N/USA/43, at 20 (Supporting Table DS:6) (Exhibit Bra-47)

146. Brazil acknowledges that there are some interaction effects that may increase or decrease the overall effects of the subsidies (Brazil's further submission, para. 225). How would your analysis under Articles 5(c) and 6.3 of the SCM Agreement and Article XVI of GATT 1994 differ if it excluded, for example, crop insurance subsidies, PFC and/or direct payments? BRA

147. Does the US agree that subsidies provided under the marketing loan programme, counter-cyclical payments and market loss assistance are or were more than minimally trade-distorting? If so, please elaborate on the type of effects which are more than minimally trade-distorting within the meaning of Annex 2 of the Agreement on Agriculture but less than adverse effects within the meaning of Article 5 of the SCM Agreement. US

63. The issues of whether a measure is more than minimally trade-distorting and whether a measure has adverse effects require two different analyses. While it may be a necessary condition that a subsidy has trade- or production-distorting effects in order to find that it causes adverse effects, it is not a sufficient condition. The question under an adverse effects analysis is one of the effect on a particular Member's "interests" – for example, whether injury to the domestic industry of another Member, nullification or impairment, or serious prejudice to the interests of another Member. Therefore, the mere showing that a subsidy can distort trade or production does not necessarily mean it has, for example, seriously prejudiced a particular Member's interests.

64. Marketing loan payments, counter-cyclical payments, and market loss assistance payments provide different types of support that can be expected to have different effects. As noted in the US answer to Question 127, the United States notifies marketing loan payments as product-specific amber box support. These payments are linked to production of upland cotton in favour of the producers of upland cotton – a producer must have harvested cotton to receive the payment. Therefore, the United States considers that marketing loan payments could not satisfy the general and policy-specific criteria set out in Annex 2 of the Agreement on Agriculture and therefore could not be deemed to have met the fundamental requirement of that Annex.

65. That a particular support measure does not conform to the general and policy-specific criteria of Annex 2 is relevant to the type of support it is deemed to be, which has meaning for a Member's compliance with its reduction commitments. That a particular measure is not green box, however, would not suffice to demonstrate that a measure has "adverse effects" within the meaning of Articles 5 and 6 of the Subsidies Agreement. A finding that a subsidy has caused adverse effects is a fact-intensive analysis. In the case of a claim of serious prejudice, for example, one of the four effects set out in Article 6.3 must be demonstrated (such as significant price suppression or depression by the subsidized product in the same market as the non-subsidized product is found) and the effects caused by the subsidy must rise to the level of "serious prejudice." Such a fact-intensive analysis must take into account, *inter alia*, the nature and amount of the subsidy, market conditions, and other factors affecting production, consumption, and prices.

66. Therefore, a conclusion that a measure does not provide green box support and therefore would not be deemed to have no or at most minimal trade-distorting effects or effects on production cannot take the place of the fact-intensive examination required to show causation under the WTO Agreements. For example, marketing loan payments provide a revenue floor of 52 cents per pound for US upland cotton producers. The effect of this subsidy would depend in large part on the producer's expected market revenue at the time of planting – that is, whether this expected revenue was above or below 52 cents per pound. Thus, the effect of this subsidy would be quite different from a subsidy that merely provided an unchanging per unit payment (e.g., 10 cents per pound), even if as a result of prices that actually develop over the course of a marketing year the per-unit payments under these two measures turn out to be the same. As another example, a measure that provided, in the aggregate, \$1 of support linked to production of upland cotton could not satisfy the general and

policy-specific criteria of Annex 2 of the Agreement on Agriculture³², but it would be difficult to conceive that the effect of \$1 in subsidies could be “significant price suppression [or] price depression” or “an increase in the world market share of the subsidizing Member” given the large number of market participants (including cotton producers worldwide), highly developed cotton markets, and volume and value of cotton trade.

67. With respect to counter-cyclical payments under the 2002 Act, the United States recalls that according to Brazil’s interpretation of the first sentence of Annex 2 as a stand-alone requirement, if a measure has no more than minimal trade-distorting effects or effects on production, it follows that such a measure must be deemed green box. As the United States has demonstrated, the economic literature on decoupled payments (counter-cyclical payments are decoupled from production although linked to current prices) suggests that the effects on production of such income transfers are no more than minimal.³³ Therefore, although the United States would not contend that counter-cyclical payments conform fully to the policy-specific criteria in Annex 2, there is not only no evidence that such payments have more than minimal trade-distorting effects or effect on production, but the evidence suggests the contrary. In such a case, the effect of a payment that does not have more than minimal effects on production would not appear to be “significant price suppression [or] depression” or an “increase in the world market share of the subsidizing Member”, much less “serious prejudice”.

68. The expired market loss assistance payments were ad hoc payments made during the 1999, 2000, and 2001 marketing years to holders of base acreage. These payments were not linked to production – that is, a recipient need not have produced upland cotton or any crop at all in order to receive the payment.³⁴ However, because these payments were explicitly made in reaction to low commodity prices, the United States considered that these payments would not conform fully to the criteria in Annex 2 of the Agreement on Agriculture and therefore notified these payments as non-product-specific amber box support. As noted above with respect to the 2002 counter-cyclical payments, however, the economic literature on payments decoupled from production suggests that the effects on production of income transfers such as the market loss assistance payments are no more than minimal.³⁵ Therefore, the evidence suggests that the effect of such payments could not be “significant price suppression [or] depression” or an “increase in the world market share of the subsidizing Member” resulting in “serious prejudice”.

148. How should the significance of price suppression or depression be assessed under Article 6.3(c) of the SCM Agreement? In terms of a meaningful effect? Or another concept? BRA, US

69. As the United States has previously noted³⁶, in Article 6.3(c) the term “significant” modifies the phrase “price suppression or depression”, suggesting that it is the level of price suppression or depression itself that must be “important, notable” or “consequential”.³⁷ As Brazil agrees³⁸, important

³² For example, the measure would not qualify as decoupled income support because, by requiring that recipients have produced upland cotton, the amount of the payment would be “related to, or based on, the type or volume of production . . . undertaken by the producer in any year after the base period”. See Agreement on Agriculture, Annex 2, para. 6(b).

³³ See, e.g., US Rebuttal Submission, paras. 59-64.

³⁴ Supplemental legislation authorizing each of these payments was passed several months after planting for the crop year in question had occurred. Even if producers had some expectations of payment at planting time, they were eligible to receive such a payment regardless of what crop they planted. Indeed, they could choose not to plant and still be eligible for the payment. This would argue that market loss assistance payments, like production flexibility contract payments, direct payments, and counter-cyclical payments, are decoupled from planting decisions.

³⁵ See, e.g., US Rebuttal Submission, paras. 59-64.

³⁶ US Opening Statement at the Second para. 58.

³⁷ US Further Submission, para. 83.

³⁸ See Brazil’s Further Submission, para. 88 (“This interpretation of price suppression and price depression is consistent with the *relevant context of Article 6.3(c)*, which includes Article 15.2 of the SCM

context for interpreting this phrase can be found in Article 15.2 of the Subsidies Agreement, which sets out for countervailing duty purposes the same effects found in Article 6.3.³⁹ This text confirms that the relevant analysis is whether the level of price suppression or depression itself is “significant”:

With regard to the effect of subsidized imports on prices, the investigating authorities shall consider whether there has been a significant price undercutting by the subsidized imports as compared with the price of a like product of the importing Member, or whether the effect of such imports is otherwise *to depress prices to a significant degree or to prevent price increases*, which otherwise would have occurred, *to a significant degree*.⁴⁰

Thus, Article 15.2 provides contextual support for reading the term “significant price suppression [or] depression” in Article 6.3(c) according to the ordinary meaning of its terms – that is, it is the degree of price suppression or depression itself that must be “significant”.

70. As suggested by this analysis, it is not the effect on the producers of the complaining Member that must be “significant”. In determining whether the alleged price suppression or depression is “important” or “notable”, it will of course be relevant to look at that suppression or depression in the context of the prices that have been affected – that is, at the *degree* of suppression or depression. One absolute level of suppression or depression could be significant in the context of prices for one product but not for another and meaning must be given to the phrase “in the same market”.

149. What is the meaning of "may" in the chapeau of Article 6.3(c) in the context of Brazil's assertion that there is no need to conduct a distinct analysis of "serious prejudice" under Article 5(c) after having made a finding under 6.3(c) or (d)? (Brazil's further submission, paras 437 ff). How, if at all, are Articles 6.2 and 6.8 relevant in this context? What context should the Panel use for assessing serious prejudice under Article 5(c) of the SCM Agreement if the Panel takes the view that Article 6.3(c) and (d) are permissive conditions for a determination of serious prejudice? US

71. The chapeau of Article 6.3 states that “[s]erious prejudice in the sense of paragraph (c) of Article 5 may arise in any case where one or more of the following apply”. The Article then goes on to detail four effects that “may” result in serious prejudice arising. Brazil’s reading would re-write the chapeau of Article 6.3, changing the permissive “may” into the obligatory “shall”. The ordinary meaning of “may” is “to express possibility, opportunity, or permission”.⁴¹ Therefore, the ordinary meaning of the chapeau of Article 6.3 would be that there is a “possibility” or “opportunity” for serious prejudice in the sense of Article 5(c) to arise where one or more of the effects listed in Article 6.3 is found.

72. Article 6.2 clarifies that a prerequisite for a finding of serious prejudice is that at least one of the four effects in Article 6.3 must be demonstrated. That is, Article 6.2 precludes a panel from finding serious prejudice (“serious prejudice shall not be found”) if a subsidizing Member demonstrates that the subsidy has not had any of the effects listed in Article 6.3. This provided a subsidizing Member with a means to overcome the presumption created through the operation of

Agreement. That provision discusses standards for the determination of injury in countervailing duty cases and provides that the investigating authorities should consider whether the effect of imports is ‘to depress prices’ or ‘to prevent price increases, which otherwise would have occurred . . . [.]’ (emphasis added).

³⁹ Effects on prices form one part of a determination of injury for countervailing duty purposes. Pursuant to Article 15.1, such a determination of injury involves an objective examination of (a) the volume of subsidized imports and the effect of the subsidized imports on prices in the domestic market for like products and (b) the consequent impact of these imports on the domestic producers of such products.

⁴⁰ Subsidies Agreement, Article 15.2 (italics added).

⁴¹ *The Random House Dictionary of the English Language, Unabridged Edition* at 886 (1983).

Article 6.1 while that provision was still in effect. However, Article 6.1 demonstrates that Members knew how to create a presumption of serious prejudice: they did so by explicitly stating that, in certain cases, “[s]erious prejudice . . . *shall be deemed to exist*” (italics added). Article 6.2, while providing a means to rebut that presumption, does not by its terms establish that serious prejudice “shall be deemed to exist” if one of the effects in Article 6.3 exists.

73. Article 6.4 lends further contextual support to the interpretation that the use of the term “may” in the chapeau of Article 6.3 signifies that the effects listed in Article 6.3 are permissive conditions for a determination of serious prejudice. Article 6.4 states that “displacement or impeding of exports shall include any case in which, subject to the provisions of paragraph 7, it has been demonstrated that there has been a change in the relative shares of the market to the disadvantage of the non-subsidized like product”. Thus, given certain situations further explained in Article 6.4, displacement or impeding of exports “shall” exist. However, Article 6.3 does not state that, given those situations, displacement or impeding of exports *resulting in serious prejudice* shall exist. That is, the situations in Article 6.4 which must result in a finding of displacement or impeding of export do not, by the terms of the Article, also result in a finding of serious prejudice.

74. Article 6.5 similarly defines a situation in which “price undercutting” under Article 6.3(c) “shall” be found but does not also mandate a finding of serious prejudice. Had Members intended (as Brazil contends) that a finding under Article 6.3 would necessarily suffice to demonstrate serious prejudice, one also would have expected Articles 6.4 and 6.5 to mandate a finding of serious prejudice where a finding of one of the effects under Article 6.3 is mandated.

75. Article 6.8 provides further contextual support for reading Article 6.3 as setting out certain permissive conditions that could result in a panel finding that serious prejudice to the interests of a Member exist. Article 6.8 states that, “in the absence of circumstances referred to in paragraph 7”, which merely preclude a panel from finding displacement or impediment resulting in serious prejudice, “the existence of serious prejudice *should be* determined on the basis of the information submitted to or obtained by the panel” (italics added). Again, this provision does not mandate a finding of serious prejudice should one or more of the effects set out in Article 6.3 be demonstrated. Rather, it emphasizes that “the existence of serious prejudice” (rather than the existence of one of the effects in Article 6.3) “should be determined” by the panel based on the information before it. Thus, while a panel may be *precluded* from making a finding of serious prejudice (where, for example, a complaining party has only alleged displacement or impediment under Article 6.3, but one of the conditions in Article 6.7 exist), there is no currently effective provision under which a panel is *compelled* to find serious prejudice.

150. Is the list in Article 6.3 of the SCM Agreement exhaustive, or could serious prejudice arise in circumstances other than those listed in paragraphs (a) through (d)? US

76. Article 6.3 sets out four circumstances in which the effects of subsidies “may” give rise to a finding of serious prejudice. Article 6.2 establishes that “serious prejudice shall not be found” if a subsidizing Member demonstrates that a challenged subsidy has not resulted in any of those four effects. Therefore, Articles 6.3 and 6.2 indicate that serious prejudice may not be deemed to have arisen without at least one of the four effects listed in Article 6.3 having been demonstrated.

151. Where in the text of Article 6.3(d) of the SCM Agreement is there a basis to take into account that 1998 may be a "misleading" year for the purposes of comparison? For example, unlike the text of Article XVI:3 of the GATT 1994, there does not seem to be a general reference to "special factors". US

77. Article 6.3(d) requires that a complaining party demonstrate that the effect of a challenged subsidy is an increase in the world market share in a particular subsidized primary product or commodity as compared to the average share it had during the previous period of three years and this

increase follows a consistent trend over a period when subsidies have been granted. Where the evidence offered by a complaining party relies in large part on abnormal production and trade data evidently caused by factors unrelated to the challenged subsidy (in the case of the United States in 1998, severe drought and record abandonment of planted acres), use of that data cannot satisfy the complaining party's burden of demonstrating causation – that is, the “effect of the subsidy”.

78. Article 6.3(d) sets out a fairly mechanical two-part test: first, there must be an increase in world market share as compared to the average over the preceding period of three years. Thus, assuming *arguendo* that Brazil could challenge expired marketing year 2001 support measures, this test would compare the world market share of US upland cotton in that year to the average over the preceding three years. Brazil, however, has misinterpreted Article 6.3(d) and examined the US world *export* share.

79. The second part of the test is that any such increase over the average of the preceding three-year period “follows a consistent trend over a period when subsidies have been granted”. The marketing year 2001 payments challenged by Brazil were first introduced for the 1996 marketing year by the 1996 Act. Thus, Brazil must demonstrate that the alleged increase in world market share follows a “consistent trend” between marketing years 1996-2001. In fact, there is no consistent trend showing an increasing US world market share over this period; that world market share has been inconsistent but showing a tendency to decline over that period. As demonstrated in Exhibit US-47, US world market share surpassed 20 per cent in both marketing years 1996 and 1997 but has not thereafter.

80. Finally, as the United States has noted in its further submission, Brazil has limited its claim under Article 6.3(d) to alleged effects in marketing year 2001.⁴² Thus, there can be no finding that challenged US subsidies under the 2002 Act presently cause serious prejudice within the meaning of Article 6.3(d). As the United States has previously noted, moreover, payments with respect to marketing year 2001 expired with the granting of support in respect of the 2002 marketing year's production, which began on 1 August 2002 – that is, seven months before this Panel's terms of reference were established. The result is that Brazil is asking the Panel to make findings and a recommendation with respect to subsidies that had been replaced at the time of panel establishment and that no longer exist to be withdrawn even were a recommendation to be made.

152. If the US is correct in asserting that the Article 13(b)(ii) Agreement on Agriculture analysis is a year-by-year analysis, how would this affect the Panel's examination of Brazil's claims of serious prejudice, including the three year period and the trend period in Article 6.3(d) of the SCM Agreement? US

81. Article 13(b)(ii) exempts from action measures that, *inter alia*, conform fully to the provisions of Article 6 of the Agreement on Agriculture. Chief among those provisions is the obligation that a Member remain within its Annual and Final Bound Commitment Levels for its Aggregate Measurement of Support, a commitment that is expressed by year. Therefore, while a Member may breach the Peace Clause in a given year by exceeding its bound commitment level, that Member may in the following year not breach the Peace Clause if its domestic support measures once again do not exceed its commitment levels. Thus, to gauge whether domestic support measures have breached the Peace Clause requires a year-by-year analysis.⁴³

⁴² US Further Submission, para. 100.

⁴³ Brazil agrees that the Peace Clause requires a year-by-year comparison. Brazil insists, however, that once a Member has breached the Peace Clause once, that Member can never thereafter regain Peace Clause protection. There is nothing in the text of the Peace Clause that supports Brazil's view on this point – nor, as a result, has Brazil pointed to any supporting text.

82. The year-by-year analysis under the Peace Clause does not affect how the Panel would undertake a serious prejudice analysis; it affects only the Panel's analysis of which of the US measures that Brazil has challenged may be the subject of the serious prejudice analysis. In the event, Brazil has only claimed that the effect of US subsidies in marketing year 2001 was inconsistent with Article 6.3(d). Therefore, the Panel's task is first to analyze whether US domestic support measures in marketing year 2001 breached the Peace Clause. If so, then the Panel would be able to undertake a serious prejudice analysis – and that second analysis is distinct from the first one. The United States has demonstrated that US measures in marketing year 2001 do not grant product-specific support to upland cotton in excess of that decided during the 1992 marketing year, whether measured according to the level of support granted by those measures or a price-gap AMS calculation.

83. With respect to the two-part test of the three-year average and consistent trend over a period when subsidies have been granted, the Peace Clause would have no impact on these tests. That is, assuming *arguendo* that marketing year 2001 measures were not exempt from action, the fact that the Peace Clause exempts from action measures for other marketing years would not preclude the Panel from examining data and evidence from those years as part of its serious prejudice analysis of the 2001 measures. The payments made in those other marketing years (that is, the marketing year 1999 measures and the marketing year 2000 measures) would be exempt from action; evidence relating to those years would not be sheltered from examination by the Panel in its serious prejudice analysis of the 2001 measures.

153. Would the conditions in Article 6.3(d) of the SCM Agreement be satisfied in respect of time periods other than the one specified? What relevance, if any, would this have for Brazil's claims? BRA

154. Does the US agree that upland cotton is a "primary product or commodity" within the meaning of Article 6.3(d) of the SCM Agreement? (ref. Brazil's further submission, para. 262) and within the meaning of Article XVI:3 of the GATT 1994? US

84. Yes.

155. Please respond to Brazil's identification of the seven-year period beginning with MY1996 (following the passage of the FAIR Act of 1996) as the "most representative period" for the purposes of Article 6.3(d)? (ref. Brazil further submission, para. 269) US

85. Brazil has challenged only those US subsidies that allegedly had the effect of increasing US world market share in marketing year 2001 – that is, marketing year 2001 payments. The second part of the test under Article 6.3(d) is that any increase in world market share that is the effect of the challenged subsidy over the average of the preceding three-year period “follows a consistent trend over a period when subsidies have been granted”. The marketing year 2001 payments were granted under the 1996 Act. Therefore, the “period when subsidies have been granted” for purposes of an analysis of the effect of marketing year 2001 support would be the marketing year 1996-2001 period.

86. The United States believes that marketing year 2001 support cannot cause present serious prejudice because these payments expired when marketing year 2002 payments began to be made. Nonetheless, if marketing year 2001 payments are the challenged measures for purposes of Brazil's Article 6.3(d) claim, there is no basis to include marketing year 2002 within the period when subsidies have been granted. (We also note that Brazil identifies a seven-year period beginning with marketing year 1996 but presents data only for the six-year period through marketing year 2001.)

156. Does the US agree that "...footnote 17 [of the SCM Agreement] does not carve out upland cotton from the scope of Article 6.3(d) of the SCM Agreement"? (ref. Brazil further submission, para. 275). US

87. The United States is not aware of any "other multilaterally agreed specific rules apply to the trade in the product or commodity in question" within the meaning of footnote 17 to Article 6.3(d) of the Subsidies Agreement.

157. Does the reference to "trade" in footnote 17 of the SCM Agreement have any impact on the interpretation of "world market share" in Article 6.3(d)? If so, what is it? US

88. The use of the term "trade" in footnote 17 provides useful context in interpreting the phrase "world market share" in Article 6.3(d). Specifically, Article 6.3(d) speaks of an increase in a Member's "world market share", not an increase in a Member's "world trade share". By using the term "market" and not "trade", Article 6.3(d) establishes that its scope is *not* limited to cross-border movements of a primary product or commodity. That is, the "world market" for a primary product or commodity encompasses all the markets in the entire "world", including the market of the allegedly subsidizing Member. Had Members desired instead to restrict the analysis under Article 6.3(d) to cross-border shipments, they could have used the phrase "world trade share" or, in Brazil's preferred formulation, "world export share", or even (as in GATT 1994 Article XVI:3) "world export trade". They did not. Finally, we note that, rather than elaborating on the test under Article 6.3(d), footnote 17 was intended to describe those products or commodities *not* covered by Article 6.3(d) and therefore could use the term "trade".

158. Please respond to Brazil's assertion that "...the absence of any payment, production or expenditure limitations in the US marketing loan programme is analogous to the EC sugar regime that was challenged in EC - Sugar Exports II (Brazil) and EC - Sugar Exports I (Australia)." (ref. Brazil further submission, para. 317) US

89. The EC sugar export regime challenged by Australia and Brazil under the GATT 1947 was manifestly different than the US marketing loan programme, primarily in that the challenged programme was an export subsidy providing export refunds on exportable surpluses of sugar. The *Sugar Exports* panel concluded that in the particular market situation prevailing in 1978 and 1979, the EC system had caused serious prejudice to Brazil's interests because it had been applied in a manner which contributed to depress sugar prices. The panel also concluded that the lack of "pre-established effective limitations" on those export refunds and the application of that refund system "constituted a permanent source of uncertainty in world sugar markets and therefore constituted a threat of serious prejudice. The panel's finding on serious prejudice was made carefully, circumscribed by "the particular market situation prevailing in 1978 and 1979". However, the panel's finding on threat of serious prejudice was made without any explanation and apparently without argument by the parties. Therefore, it is difficult to see how the Panel could draw useful guidance from this finding by that panel or draw conclusions on relevant types of payments.

159. The EC, in its oral statement (paras 9 and 10), disagrees with the US interpretation of the terms "same market". Can the US comment on the EC's view? US

90. The United States still has difficulty with the EC view. The United States cannot understand how the "world" can be one "market" for purposes of Article 6.3(c), which by its nature calls for a comparison of the prices of the goods of one Member when competing in a market with the goods of another Member. Goods are not sold to the "world" – they are sold in the market of a particular country.

91. The EC on the other hand evidently considers that it is at least possible that the world could function as one market and therefore constitute a "same market" for purposes of analyzing whether

the “effect of the subsidy” is “significant price suppression [or] depression” of the price of a non-subsidized product in the same market. For the reasons set forth in the US further submission, the United States considers that such an interpretation would render the “in the same market” language inutile because the subsidized and non-subsidized products could never be found in the same geographic market and still be considered to be in the same “world market”. Furthermore, under the EC's approach, a Member could be selling at a price well above another Member's price in the same country, and yet be found to be depressing prices on the "world market" due to a comparison between sales prices of the Member in one country compared to sales prices of the other Member in a different country.

92. However, the EC itself concedes that a “world market” could only be deemed to exist if there were not significant barriers to trade in the product at issue, such as customs duties, technical barriers to trade, etc. The EC’s own explanation suggests that such a “world market” is unlikely to exist because of significant barriers to trade somewhere in the world. Thus, even under the EC’s approach, it is not the case that there is a “world market” for upland cotton.

160. Without prejudice to the meaning of "world market share" as used in Article 6.3(d) of the SCM Agreement, can you confirm the world export share statistics provided in Exhibit BRA-206? US

93. The table below reflects most recent updates for 2002-03 and 2003-04. We caution that, as noted in the footnotes in the table, the data are drawn from different sources and data sets. Also, we have corrected data in BRA-206 for 1997-98 for total world exports, world upland exports, and US export share.

World cotton exports (million bales)

Year	US upland exports (1)	Total world exports (2)	ELS world exports (3)	World upland exports (4)	US Share of World Exports (5)
1996-97	6.399	26.929	1.017	25.912	24.70%
1997-98	7.06	26.838	1.106	25.732	27.44%
1998-99	4.01	23.668	1.085	22.583	17.76%
1999-00	6.303	27.326	1.193	26.133	24.12%
2000-01	6.303	26.589	1.127	25.462	24.75%
2001-02	10.603	29.052	1.325	27.727	38.24%
2002-03	11.266	30.629	1.989	28.640	39.34%
Average: 98/99 - 00/01	5.539	25.861	1.135	24.726	22.40%
99/00 - 01/02	7.736	27.656	1.215	26.441	29.26%
00/01 - 02/03	9.391	28.757	1.480	27.276	34.43%

Source:

(1) *USDA, Fact Sheet Upland Cotton, 2003 p.5*

(2) *USDA, ERS. Cotton and Wool Yearbook, 2002, p. 31; Fact Sheet Upland Outlook, USDA, Oct 2003 table 2*

(3) *ICAC, Cotton World Statistics, Sept. 2003, p. 7.*

(4) *Calculation: (2) - (3)*

(5) *Calculation: (1)*100/(4)*

161. Would a finding of serious prejudice under Article 5(c) of the SCM Agreement be determinative for a finding under Article XVI:1 of the GATT 1994? Why or why not? What, if any, is the role of footnote 13 of the SCM Agreement in this context? BRA, US

94. Article 5(c) establishes that one of the adverse effects that a subsidizing Member should not cause to the interests of other Members is “serious prejudice”, and footnote 13 to that Article states that the term ““serious prejudice to the interests of another Member” is used in the same sense as it is used in paragraph 1 of Article XVI of GATT 1994”. Therefore, “serious prejudice” under Subsidies Agreement Article 5(c) and GATT 1994 Article XVI:1 must be read to have the same meaning. As Article 5(c), and Article 6 which explains it, are the more detailed provisions on “serious prejudice” and contain a more effective remedy than the consultation envisioned under GATT 1994 Article XVI:1, the Panel’s analysis should begin with the Subsidies Agreement provisions. Were the Panel to agree that Brazil has not established that the effect of the challenged subsidy is “serious prejudice” within the meaning of the Subsidies Agreement, it would be difficult to see how the Panel could then determine that “serious prejudice” exists within the meaning of GATT 1994 Article XVI:1 since the term is used “in the same sense” in these provisions.

162. Can the US confirm that marketing loan/LDP, step 2 and counter-cyclical payments are mandatory if the price conditions are fulfilled? US

95. The statutory authority for marketing loan payments, step 2 payments, and counter-cyclical payments does not provide the Secretary with the authority to arbitrarily decline to make these payments to qualified recipients. However, certain conditions must be met before these payments will be made: price conditions must be met, the producer must meet all conditions for payment, including compliance with "sodbuster" and "swampbuster" provisions and any planting restrictions, the Commodity Credit Corporation (CCC) must not have exhausted its statutory borrowing authority, and Congress must not have cut back on the programme, by an appropriations bill or otherwise.

96. As the question notes, different price conditions apply to each of these payments. For example, in the case of marketing loan payments, the adjusted world price (as calculated by the Department of Agriculture) must be below 52 cents per pound. Recently, the adjusted world price has been above 52 cents per pound and thus no marketing loan payments have been made to qualified recipients.

97. There is no preset limit on the total amount of payments that can be made under each of these programmes although for counter-cyclical payments a maximum total outlay can be calculated using the base acres, base yields, and maximum payment rate for each commodity produced during the historical base period. In addition, for certain recipients, per-person payment limits may apply. We also note that under Section 1601(e) of the 2002 Act, the Secretary has the authority (so-called "circuit breaker" authority) to make adjustments to farm programmes because of WTO domestic support reduction commitments. Presumably, this authority could result in refusals to make certain payments.

98. Conditions for receiving counter-cyclical and marketing loan payments are numerous. The programme contract for counter-cyclical payments is required by section 1105 of the 2002 Act. That section provides explicitly that the producers must agree: (A) to comply with the requirements dealing with the highly erodible cropland conservation found at 16 USC 3811 *et seq.*; (B) comply with the wetland conservation requirements found at 16 USC 3821 *et seq.*; (C) comply with the planting flexibility requirement of Section 1106 of the 2002 Act; (D) use the land representing the base acres for an agricultural or conserving use but not for a non-agricultural, commercial, or industrial use, as determined by the Secretary; and (E) control noxious weeds and otherwise maintain the land in accordance with sound agricultural practices as determined by the Secretary of Agriculture, if the agricultural or conserving use involves the noncultivation of any portion of the land as permitted under the specification just set out in (D). For marketing loans, the loan agreement and loan

regulations, contained in 7 CFR part 1421, specify various conditions that must be met and followed by the producer. Under 16 USC 3811 *et seq.*, the wetland and conservation provisions cited above are made applicable to all commodity benefits, including loans.

163. Are US cotton producers able to cover the fixed and variable costs without subsidies? Please provide substantiating evidence. Of what relevance is this, if any, to Brazil's actionable subsidy claims? US, BRA

99. The United States notes that even using cost data that reflects 1997 cost structures⁴⁴, US producers appear to have been able to cover variable costs through the sale of cotton at harvest time in every year but marketing years 2001 and (more narrowly) 2002. In this, US producers were no different than Brazil's farmer witness, Christopher Ward, who stated: "But even with these high yields and the excellent quality of our land, we were not able to fully recover all of our variable costs of production during the 2000/01 and 2001/02 seasons[,]” a position evidently shared by most producers in Mato Grosso, Brazil's leading cotton-producing state.⁴⁵

100. Furthermore, even in years in which US producers may not have been able to cover fixed and variable costs, it does not follow that it is subsidies that covered these costs. Again, Mr. Ward explained that in marketing years 2000 and 2001, "Nor were we able to meet our total costs which include the additional fixed costs." Therefore, producers can cover costs from revenue sources other than subsidies. That harvest prices at times fall below costs does not necessarily mean that subsidies have had the effect of maintaining production.

US upland cotton operating costs compared to harvest cotton price

Year	Cotton price at harvest (\$/lb)	Average operating cost (\$/lb)
1998	0.64	0.481
1999	0.47	0.418
2000	0.57	0.473
2001	0.35	0.447
2002	0.42	0.453

Source: USDA, Economic Research Service, Agricultural Resources Management Survey (www.ers.usda.gov/data/costsandreturns/testpick.htm)

K. CAUSATION

164. When the US points, in its oral statement of 7 October, to the alleged "bias" of Prof. Sumner's model, is it arguing that US subsidies are irrelevant to the movement in prices and production (acreage) of upland cotton? US

101. The United States recognizes that subsidies can potentially affect production and prices of upland cotton. The question is one of the nature of the subsidy examined and the degree of any predicted effect, which could range from significant to negligible. The criticisms of Dr. Sumner's model outlined in the US oral statement of October 7, 2002 take issue with many of the underlying

⁴⁴ Recall that the Department of Agriculture conducted a survey of cotton farmers in 1997. For any cost data published by the Department since that time, the 1997 data has merely been updated by applying the producer price index to 'update' input costs. See US Closing Statement at the Second Session of the First Panel Meeting, paras. 10-11.

⁴⁵ Statement of Mr. Christopher Ward at the Second Session of the First Panel Meeting, para. 6 (emphasis added). Mr. Ward goes on to state: "Based on my discussions with many producers relating to Mato Grosso cotton production and revenue, I know that most other producers in State of Mato Grosso were in the same situation as we were during the 1999-2000 period." (*Id* (emphasis added))

assumptions in the model, particularly in regards to how decoupled payments were modelled and the choice of baselines used by Dr. Sumner, which have led to results that have exaggerated the impact of US subsidies on world cotton markets.

165. Please comment (and submit substantiating evidence) on the US assertion that the FAPRI model has been designed and developed for prospective analysis, and is not suitable for retrospective counterfactual analysis. What is the reliability of past FAPRI-produced analyses when compared with actual data for the period covered by them? Is there any other instrument that can be used to try to identify the effect of subsidies already granted, or of their removal? BRA, US

102. FAPRI uses its models for prospective analyses; that is, they analyze the future effects of proposed programme changes against a baseline that assumes current programmes are in place. Recent examples of FAPRI analyses include the effects of stricter payment limitations on US farmers⁴⁶, an analysis of the European Union's 2003 CAP Reform Agreement⁴⁷, and the effects on the US dairy industry of removing current Federal regulations.⁴⁸ These analyses are forward-looking examinations of the effects of policy changes.⁴⁹

103. Econometric modelling systems similar to the ones maintained by FAPRI and USDA are designed for prospective analyses of alternative policy assumptions. The foundation for forward-looking analyses is the baseline projections, which are conditioned on specific assumptions for exogenous variables, i.e., those that are independent of the modelling system. The baseline model is also conditioned to incorporate the current structure of specific commodity markets through equation specifications, elasticity estimates, and structural shift and dummy variables. As a result, the baseline models will not be appropriately structured to analyze changes over a historical period. For example, models calibrated for the current structure of the US textile industry may not be appropriate to assess the structure present in the late 1990's due to the tremendous changes that have occurred. Another difficulty of using the system over a historical period is the degree of external shocks that impact the model. In prospective analysis, assessing the impacts of alternative policies occurs absent of extreme shocks from independent variables.

⁴⁶ FAPRI. *FAPRI Analysis of Stricter Payment Limitations* FAPRI-UMC Report #05-03 17 June 2003. 15 pp. Available at: http://www.fapri.missouri.edu/FAPRI_Publications.htm.

⁴⁷ FAPRI. *Analysis of the 2003 CAP Reform Agreement*. FAPRI Staff Report #2-03, 9 September 2003. 16 pp. Available at: http://www.fapri.missouri.edu/FAPRI_Publications.htm

⁴⁸ FAPRI. *The Effects on the United States Dairy Industry of Removing Current Federal Regulations*. FAPRI-UMC Report #03-03. April 2003. 14 pp. Available at http://www.fapri.missouri.edu/FAPRI_Publications.htm

⁴⁹ FAPRI recognizes the forward-looking nature of its analyses and the limitations of those baselines quite clearly:

Each year, FAPRI prepares a set of baseline projections that provide information about the outlook for agricultural markets, farm programme spending, farm income, and a variety of other indicators. The baseline then serves as the point of comparison for analyses of alternative policy options....

The baseline is not a forecast of what will happen, but rather a projection of what could happen under a particular set of assumptions. Current global policies are held in place, even when there is reason to suspect changes are likely....

In reality, these assumptions are certain to be violated and actual market outcomes will differ from the deterministic baseline projections presented in the supply-demand tables....

104. As mentioned by Dr. Sumner in Annex I to Brazil's submission of 30 September, baseline models such as the one utilized by FAPRI or USDA are not forecasting models. They are used to analyse proposed policy changes.⁵⁰ The attached table shows the forecast accuracy for year ahead price forecasts by FAPRI.

FAPRI farm price projections for upland cotton compared to actual prices, MY1999-2003 (\$/lb)

FAPRI published baseline	Marketing year	FAPRI projected price	Actual price 1/	Difference 2/
January 1998	1999/00	0.689	0.45	-0.239
January 1999	2000/01	0.531	0.498	-0.033
January 2000	2001/02	0.479	0.298	-0.181
January 2001	2002/03	0.554	0.43	-0.124
January 2002	2003/04	0.385	0.463 3/	0.078

Source: FAPRI, USDA World Agricultural Supply and Demand Estimates

1/ Marketing year average farm price reported by USDA.

2/ Actual farm price minus forecast price

3/ Average cotton farm price for August 2003. USDA is prohibited from publishing cotton price forecasts.

105. One potential approach to using a baseline model to estimate the effects of subsidies during a historical period would be to use an *ex post* prospective analysis. Under an *ex post* analysis, instead of using the current baseline for measurement, one would use a past baseline to make year-ahead projections of the effects of subsidies on the cotton market. For example, to analyze the effects of subsidies on the 1998/99 marketing year, one could use the January 1998 FAPRI baseline model to project the effects of removing subsidies and compare them to baseline levels for the 1998/99 marketing year. To analyze the 1999/00 marketing year, one would update the baseline to the January 1999 baseline and so on, until the current baseline. This would provide baseline comparisons that would reflect the estimated effects of the programmes at the time of planting in each year.

166. The US states that "futures prices demonstrate that market participants predict increasing upland prices over the course of the marketing year" (US 7 October oral statement, para. 62). Please elaborate on this argument including citing specific futures prices. US

106. Exhibit US-68 shows average daily closing prices for the December 2003 cotton futures contract. Daily futures prices for December 2003 and May 2004 delivery have increased by as much as 35 per cent from January 2003 levels.

107. Futures prices reflect a price that a buyer is willing to pay to secure a supply at a given price and protect against the possibility of prices rising even higher. Thus, where futures contract prices are higher than current market prices, the futures prices suggest that cotton buyers are concerned about

⁵⁰ For example, the US Department of Agriculture explains:

The projections are a conditional scenario with no shocks and are based on specific assumptions regarding the macroeconomy, agricultural policy, the weather, and international developments. In particular, the baseline incorporates provisions of the Farm Security and Rural Investment Act of 2002 (2002 Farm Act) and assumes that current farm legislation remains in effect through the projections period. The projections are not intended to be a Departmental forecast of what the future will be, but instead a description of what would be expected to happen under a continuation of the 2002 Farm Act, with very specific external circumstances. Thus, the baseline provides a point of departure for discussion of alternative farm sector outcomes that could result under different domestic or international assumptions."

USDA Agricultural Baseline Projections to 2012. Office of the Chief Economist, US Department of Agriculture.

the possibility of cotton prices rising still higher and are willing to lock in a purchase price that carries a premium over current prices.

108. In fact, current futures prices reveal that market participants anticipate upland cotton prices rising over the current 2003 marketing year.

New York Cotton Exchange, Closing Futures Prices MY03 Friday, 24 October 2003 ⁵¹	
December 2003 contract	82.11 cents per pound
March 2004 contract	84.34 cents per pound
May 2004 contract	84.50 cents per pound
July 2004 contract	84.64 cents per pound

That is, a producer may sell cotton futures for December delivery at 82.11 cents per pound, but for deliver later in marketing year 2003 the price rises to greater than 84 cents per pound. To update the information provided by the United States to the Panel in its further submission⁵², these futures prices indicate that the market expects cotton prices to remain well above their 20-year average of 67.86 cents per pound (1983-2002) within the current 2003 marketing year and well above what Brazil calculates as the 1980-98 A-index average (74 cents per pound) – that is, the average for the period *before* Brazil alleges serious prejudice through significant price suppression or depression.⁵³ Thus, given expected cotton prices reflected in futures contracts, Brazil has not demonstrated any clearly foreseen and imminent likelihood of serious prejudice. Quite the contrary: in marketing year 2003, upland cotton producers expect high and increasing prices.

167. How does Brazil react to Exhibit US-44? BRA

168. Please confirm that the production figures cited in Exhibit US-47 are for upland cotton only and do not include textiles. US

109. Yes, the production figures cited in Exhibit US-47 are for upland cotton production only. They do not include the raw cotton equivalent of textile production.

169. Can the US confirm the accuracy of the facts and figures cited in the four bullet points in paragraph 12 of Brazil's 7 October oral statement? US

110. From paragraph 12 of Brazil's 7 October oral statement:

Between MY 1999-2001, prices received by US upland cotton farmers fell by 34 per cent, yet US production increased by 20.3 per cent. . . .

Fact check: We can confirm the price and production figures given and would note again Brazil's selective use of marketing year 2001 as the end-point for its comparison. As Brazil complains of effects over marketing years 1999-2002, it would appear that Brazil has simply chosen to use MY2001 figures to inflate the figures it presents.

Between MY 1999-2002, the average US upland cotton farmer would have lost 24.3 cents per pound for every pound of cotton produced if revenue were based only on market revenue. The US response to this huge gap between market prices and costs was to increase

⁵¹ Current futures contract prices are available at: <http://www.nybot.com/cotton/> (click on "Futures").

⁵² See, e.g., US Further Submission, para. 118.

⁵³ Brazil's Further Submission, para. 114, figure 6.

production leading to an increase of US exports by 78.7 per cent and to an increase in the US world market share from 24.1 per cent to 41.6 per cent. . . .

Fact check: Based on Economic Research Service (ERS) estimates provided in Exhibit US-69, the market value of upland cotton (including the value of cottonseed) averaged \$325.06 per acre over MY 1999-2002. Operating costs averaged \$261.35 per acre over MY 1999-2002. The value of upland cotton production less operating costs averaged \$63.71 per acre. Based on an average upland cotton yield of 577 pounds per planted acre, upland cotton producers received 11.05 cents per pound above their operating costs.

We can confirm the export figure but note that the US share of “world exports” rose from 24.1 per cent in 1999/00 to 39.34 per cent in 2002/03. (See US response to Question 160). In addition, we note that US world market share over the marketing year 1999-2002 period fell from 18.6% in MY1999 to 16.9% in MY2000, rose to 19.8% in MY2001, and fell again to 19.6% in MY2002.⁵⁴

Between MY 1999-2001, the US dollar appreciated approximately 15 per cent against the currencies of other worldwide cotton producers. . . . US exports increased by 68 per cent. . . .

Fact check: ERS calculates a commodity-weighted exchange rate index for upland cotton based on the real exchange rates of importing countries, weighted by the share of US cotton exports.⁵⁵ Based on this index, the dollar appreciated by 6.2 per cent from 1999 to 2001. ERS also calculates a commodity weighted exchange rate index based on the currencies of other cotton producers and their share in world cotton trade. Based on this index, the dollar appreciated by 11 per cent from 1999 to 2001.

Fact check: We can confirm the US upland cotton export figure and again note Brazil’s use of marketing year 2001 for its comparison.

US costs of production are much higher than those of most other exporters of upland cotton, yet the US export market share increased from 24.1 per cent to 41.6 per cent between MY 1999-2002.

Fact check: In paras. 284 and 285 of its Further Submission of 9 September 2003, Brazil uses data from the International Cotton Advisory Committee (ICAC) to compare costs of production across countries, which represents the most complete published comparisons of costs of cotton production for major cotton producing countries. Nevertheless, even when good survey data are available for one country, using cost of production data to draw valid economic conclusions is fraught with difficulties. In fact, the ICAC specifically discourages this kind of cross-country comparison: *‘Because of a number of limitations, it is not advisable to compare the costs of production among several countries at the same time’*.⁵⁶

Fact check: Over the period 1999/00 to 2002/03, the US share of world exports rose from 24.1 per cent to 39.34 per cent. (See US response to Question 160).

170. Brazil quotes a report that states that a 10% increase in soybean prices reduces upland cotton acreage by only 0.25% (Brazil’s 7 October oral statement, para. 27). Could Brazil indicate if this analysis is done on a short-run basis or a long-run basis? BRA

⁵⁴ See Exhibit US-47.

⁵⁵ See Exhibit US-69.

⁵⁶ Raffiq Chaudhry, International Cotton Advisory Committee, “Cost of Producing Raw Cotton” Presented at the III Brazilian Cotton Congress, Brazil, 31 August 2001 (emphasis added).

171. In paragraphs 22 and 23 of its further submission, we understand that the US is, in short, claiming that increased total supply (i.e. including polyester) drove prices down. On the other hand, we note that, according to the figures in the chart in paragraph 22 of the same submission, the world production of cotton during this period has basically been steady. Do all polyester fibres as represented by these figures compete directly with cotton? That is to say, do these figures for polyester fibres include, for example, those that are used for textiles that technically cannot be substituted by cotton? US

111. The figures in the chart in paragraph 22 represent world polyester textile production. Polyester competes with cotton either directly in the fibre market or indirectly through apparel and other intermediate products.

172. Please estimate the price effect, in cents per pound, of the growth in the US retail market which it is said has directly contributed to strengthening world cotton prices. US

112. As was presented in the table in paragraph 27 of the Further Submission of the United States of 30 September 2003, US retail purchases of raw cotton fibre increased from 12.3 million bales in 1990 to 20.9 million bales in 2002, an increase of 8.6 million bales. This increase accounted for the entire increase in world retail purchases of raw cotton fibre over the same period and reflects an increase at the world level of 10 per cent. Based on the average demand elasticity of -0.25 used by Dr. Sumner in his analysis (see Annex 1 of Brazil's Further Submission to the Panel, para 23), an equivalent price decline of 40 per cent would be necessary to generate a 10 per cent increase in demand of cotton, all else held equal. Of course, this omits other factors such as supply response of world cotton producers and competition of manmade fibres. Nonetheless, it is clear that the growth in retail purchases of cotton fibres in the United States has strengthened world prices.

173. The US asserts that "burgeoning US textile imports ¼ shifted the disposition of US cotton production from domestic mills to export markets" (US further submission, para. 20). A similar description appears in paragraph 33, together with the explanation that "the share of world cotton consumption supplied by US cotton has been roughly the same since 1991/92". Why have sales of US cotton for export increased and sales of cotton imported into the US increased? US

113. The role and impact of rapidly growing US textile and apparel imports is fundamental in explaining the shift in the use of US cotton production from domestic mills to foreign mills. As noted at paragraphs 20 and 33 of the US further submission, the US textile and apparel industry has suffered from declining competitiveness compared with off-shore producers for many years, reflecting many factors, including higher wage costs, a strong US dollar, etc. As domestic mills have shut down in the United States, and production has moved overseas, domestic demand for US cotton by domestic mills has declined sharply.

114. But US consumer demand for cotton products has not declined. That demand has increasingly been met by lower-priced imports of cotton textiles and apparel. As can be seen in the table following paragraph 34 of the US further submission, US imports of cotton textiles (in cotton equivalents) have more than tripled since 1990. It is important to note that the import, export, and consumption data in that table are expressed in bales of cotton-equivalent. In other words, the data are not "sales of cotton imports", but rather represent the amount of cotton imbedded in the particular products.⁵⁷

⁵⁷ These estimates of the "cotton equivalent" of textile imports are done by USDA's Economic Research Service, based on a set of internationally-accepted conversion factors. See Cotton and Wool Situation and Outlook Yearbook. Market and Trade Economics Division, Economic Research Service. US Department of Agriculture, November 2002, CWS-2002.

115. US cotton is grown to be used to make cotton textiles and apparel. The point of the US submission is to explain how the location of where US cotton is manufactured into products has shifted. US and world consumers continue to purchase cotton products. But increasingly US consumers purchase those cotton products, made from exported US cotton, from overseas manufacturers as US manufacturers are less able to compete. That is the structural transformation that paras. 33-34 and the accompanying table seeks to present and explains at least in part some of the changes in US exports.

174. How, if at all, did the Asian financial crisis affect the United States' world market share? Did it disproportionately affect the US as compared to other exporters? US

116. The Asian financial crisis disrupted cotton consumption (spinning) in the major consuming countries of Thailand, Indonesia, and the Republic of Korea in 1997/98, reducing their mill use 9 per cent from the preceding year. In addition, the decline in world economic growth induced by the crisis reduced total world cotton consumption 3.4 per cent in 1998/99 from the pre-crisis level in 1996/97. Subsequently, however, the depreciation of currencies in these three countries boosted their cotton consumption due to expanding textile exports. World cotton consumption rose 11 per cent between 1996/97 and 2002/03, while consumption in Thailand, Indonesia, and Korea collectively rose 16 per cent. During this same period, US spinners lost market share to textile imports, due in large part to currency effects, and US domestic mill use fell 35 per cent.

117. US export share in these markets is influenced by total supply availability, qualities produced, and price. For example, US export share of the three countries' consumption fell by more than half in 1998/99, due to the drought-devastated US crop. Export share has since returned to the pre-crisis level of about 30 per cent and, with higher consumption, this added about 400,000 bales to US exports between 1996/97 and 2002/03. Since the combined total consumption increase for Thailand, Indonesia, and Korea was about 800,000 bales, this indicates that other exporters also increased exports by about 400,000 bales. As US mill use of cotton declined while exports increased, US world market share was left relatively unchanged (with a slight downward bent) by the Asian financial crisis.

175. With reference to paragraphs 57-58 and the related table on page 21 of the US further submission, could you please clarify the arguments regarding the ratio of the soybean futures to the cotton futures prices since in the table the inverse ratio is used? US

118. Attached is a corrected version of the table. The ratio of cotton futures price to soybean futures prices is positively correlated with movement in planted cotton area.

Expected cotton and soybean prices and planted cotton acreage

Year	December cotton futures (cents/lb)	November soybean futures (\$/bushel)	Ratio of cotton futures to soybean futures	Planted cotton acres (million acres)
1996	78.58	7.23	10.87	14.4
1997	76.82	6.97	11.02	13.6
1998	72.13	6.64	10.86	13.1
1999	60.32	5.11	11.8	14.6
2000	61.31	5.32	11.52	15.3
2001	58.63	4.67	12.55	15.5
2002	42.18	4.50	9.37	13.7
2003	59.6	5.26	11.33	13.5

176. With reference to Figure 4 of Brazil's Further Submission, how does Brazil explain the apparent decrease in prices in 2001 and the increase of the A-Index in recent months, despite the continued use of US subsidies on upland cotton? BRA

177. Could the United States further elaborate on paragraph 50 of its 7 October oral statement? US

119. Lin et al. estimated that the own-price elasticity of cotton acreage under the FAIR Act was 0.466.⁵⁸ This is identical to the 2003 net-return elasticity reported by Dr. Sumner. However, it is incorrect to equate a price elasticity to net-return elasticity given the linear specification utilized by Dr. Sumner. The implied price elasticity from Dr. Sumner's model would be approximately 50 per cent larger than the net-return elasticity. Larger elasticities imply greater acreage shifts to change in policies or prices.

120. The relationship between the price elasticity and a net revenue elasticity can be shown as follows. Given a linear specification as described by Dr. Sumner, then cotton area (CA) can be expressed:

$$(1) \quad CA = a_0 + a_1 * CNR + a_2 * Z,$$

where CNR is Expected Cotton Net Returns and Z is a vector of other variables including returns from competing crops.

The elasticity with respect to CNR is found by differentiating the equation with respect to CNR. The derivative is the coefficient a_1 . The elasticity, e_{NR} , is expressed as follows:

$$(2) \quad e_{NR} = a_1 * CNR / CA.$$

With CNR a function of the cotton price P, the elasticity with respect to P can be determined by taking the derivative of the equation with respect to price P. Based on equation (1) from page 13 of Annex I, the derivative with respect to price P is $a_1 * Y$, where Y is expected yield.

It follows that the price elasticity is $e_P = a_1 * Y * P / CA$. One can then conclude that $e_{NR}/e_P = ENR / (Y * P)$.

The relationship between e_{NR} and e_P can be found by looking at the relationship between CNR and $Y * P$. Specifically, $e_P = ((Y * P) / CNR) * e_{NR}$.

In recent years, the ratio of $(Y * P) / CNR$ has been approximately 1.5, implying that $e_P = 1.5 * e_{NR} = 1.5 * 0.466 = 0.699$.

178. The Panel notes Exhibit US-63. Could the US please provide a conceptually analogous graph concerning US export sales during the same period? US

121. Exhibit US-70 shows in table and graph form the per cent change over the previous year for upland cotton exports by the United States and the rest of the world. In addition, the United States provides in Exhibit US-71 a table and graph demonstrating the absolute levels of US exports and domestic consumption. As the figures show, over the last seven years domestic consumption has declined by almost the same amount by which exports have increased, leaving US world market share largely unchanged.

⁵⁸ Lin, W., P.C. Westcott, R. Skinner, S. Sanford, and D.G. De La Torre Ugarte. *Supply Response Under the 1996 Farm Act and Implications for the US Field Crops Sector*. US Department of Agriculture, Economic Research Service, Technical Bulletin No. 1888, Appendix table 21.

179. Could Brazil comment on the argument that decoupled payments and other subsidies to upland cotton are largely being capitalized into land values and that removing these subsidies would reduce the cost of production of upland cotton producers (US 7 October oral statement, para. 48). What would be the net effect of these adjustments? BRA

180. Please describe the precise formula as to how USDA determines the "adjusted world price" using the Liverpool A-Index, the NY futures price and any other relevant price indicators. Please submit substantiating evidence. BRA, US

122. The Adjusted World Price (AWP) is equal to the Northern Europe (NE) price (the 5-day average of the 5 lowest-priced growths for Middling 1-3/32 inch cotton, cost, insurance and freight [CIF] northern Europe), adjusted to US base quality and average location. The AWP for individual qualities is determined using the schedule of loan premiums and discounts and location differentials. A "coarse count adjustment" (CCA) may be applicable for cotton with a staple length of 1-1/32 inches or shorter and for certain lower grades with a staple length of 1-1/16 inches and longer. The AWP and CCA are announced each Thursday.⁵⁹

123. A Step 1 adjustment to the AWP may be made when the 5-day average of the lowest US growth quote for Middling 1-3/32 inch cotton, CIF United States-northern Europe (USNE) price, exceeds the NE price and the AWP is less than 115 per cent of the loan level. The Secretary of Agriculture may lower the AWP up to the difference between the USNE price and the NE price. A Step 1 adjustment has never been made, although the conditions have been met many times.

181. Please provide a side-by-side chart of the weekly US adjusted world price, the Liverpool A-Index, the NY futures price, and spot market prices from 1996-present. What, if anything, does this reveal? BRA, US

124. Exhibit Q181 sets out weekly price movements for the Adjusted World Price, the Liverpool A Index, the nearby New York cotton futures price and the spot market price from January 1996 to present.

182. Please explain why the US can be taken to be price leaders, or price setters, (and not just takers) when US producers receive large subsidy payment to support the difference between world prices and their own costs? BRA

L. ARTICLE XVI OF GATT 1994

183. Why does Brazil believe that the appropriate "previous representative period" is the term of the previous Farm Bill, MY1996-2002? (Brazil's further submission, para. 282) BRA

184. Why does Brazil believe that an "equitable share" is one which factors out all subsidies? To the extent that domestic support and export subsidies are permitted by the Agreement on Agriculture, why should they not be accepted as being normal conditions in analyzing an equitable market share? (See Brazil's further submission, paras 288-289) BRA

185. Please respond to the following questions concerning the relationship between Article XVI:3 of the GATT 1994, the disciplines on export subsidies and domestic support in the Agreement on Agriculture and the disciplines on prohibited export subsidies and actionable subsidies in Articles 3, 5(c) and 6.3(d) of the SCM Agreement. BRA, US

(a) Are agricultural domestic support programmes challengeable under Article XVI:3 of the GATT 1994? How, if at all, is the title of Section B of Article XVI ("Additional

⁵⁹ See Exhibit US-72.

provisions on *export subsidies*" (emphasis added)) relevant? How, if at all, are Articles 13 and 21.1, or any other provisions of the Agreement on Agriculture, relevant?

125. As indicated in the US opening statement at the recent panel meeting⁶⁰, GATT 1994 Article XVI:3 applies only to export subsidies. Paragraph 3 is found in Part B of Article XVI, entitled "Additional Provisions on Export Subsidies", as opposed to Part A, which is entitled "Subsidies in General". Paragraph 2 (also in Part B) states that "[c]ontracting parties recognize that the granting of a *subsidy on the export* of any product may have harmful effects for other contracting parties" (emphasis added). Paragraph 3 begins with the word "[a]ccordingly", the ordinary meaning of which is "[i]n accordance with the logical premises; correspondingly"⁶¹, and follows with "contracting parties should seek to avoid the use of *subsidies on the export* of primary products" (emphasis added). That is, "in accordance with" the recognition in paragraph 2 that export subsidies may have harmful effects, paragraph 3 address the use of "subsidies on the export of primary products". The second sentence of paragraph 3 follows this hortatory statement with the obligation not to apply subsidies "which operate[] to increase the export of any primary product" in a manner that "results in a contracting party having more than an equitable share of world export trade in that product". Paragraph 4 "[f]urther" addresses export subsidies for "any product other than a primary product". Thus, the text and context of paragraph 3 indicate that this provision is addressed to export subsidies and not domestic support programmes.

126. The Peace Clause provides further context supporting this interpretation. Article 13(c)(ii) exempts export subsidies that conform fully with Part V of the Agreement on Agriculture from, *inter alia*, "actions based on Article XVI of GATT 1994" – that is, including Article XVI:3 on export subsidies. Article 13(b)(ii), on the other hand, exempts conforming domestic support measures from, *inter alia*, "actions based on paragraph 1 of Article XVI of GATT 1994" but does not mention Article XVI:3. Thus, Article 13 lends contextual support to the notion that Article XVI:3 applies to export subsidies on primary products or commodities but does *not* apply to domestic subsidies on such products.

(b) Are the requirements of Article XVI:3 of the GATT 1994 reflected in, developed by or subsumed by the requirements in Article 6.3(d) of the SCM Agreement, or in any other provisions of the covered agreements? Of what relevance, if any, is the Appellate Body Report in US-FSC, para. 117 here?

127. Article 6.3(d) of the Subsidies Agreement does not, by its terms, interpret or replace GATT 1994 Article XVI:3. In fact, the range of measures potentially actionable under Article 6.3 is broader than the export subsidies subject to GATT 1994 Article XVI:3. In addition, the analysis under these two provisions is different. Article 6.3(d) is concerned with whether the effect of a subsidy is to increase the world market share of the subsidizing Member; GATT 1994 Article XVI:3 is concerned with whether export subsidies result in a Member having "more than an equitable share in world export trade" in a particular product. However, an important similarity between these two provisions is the scope of products covered by their respective disciplines. GATT 1994 Article XVI:3 is concerned with export subsidies on primary products; Article 6.3(d) is concerned with any subsidy on "a particular subsidized primary product or commodity". This similar product coverage resulted because Members desired to provide more operationally effective subsidies disciplines with respect to these products but had found the "more than equitable share" language of GATT 1994 Article XVI:3 to be unworkable. For further discussion, please see the US response to Question 186 from the Panel.

(c) Of what relevance, if any, is the fact that the definition of "subsidy" in Article 1 of the SCM Agreement and the prohibition on subsidies contingent upon export in

⁶⁰ US Opening Statement at the Second Session of the First Panel Meeting, para. 60.

⁶¹ *The New Shorter Oxford English Dictionary*, vol. 1, at 15 (1993 ed.) (third definition).

Article 3.1(a) were introduced in the Uruguay Round, but did not exist at the time that the GATT 1947 was negotiated?

128. The United States notes the Appellate Body's discussion of relevant differences between the provisions of the Subsidies Agreement and those of GATT 1994 in *United States – FSC*.

186. Could the United States please expand upon its statement that "[t]hese are the types of considerations that led to the negotiation of the Subsidies Agreement...." (US further submission, para. 109)? Is there any relevant material, including, for example, drafting history that might support this statement? US

129. Dissatisfaction with the difficulties in applying the "more than equitable share" standard of GATT 1994 Article XVI:3 was an important motivation for the negotiation of stronger and more operational disciplines in the WTO Subsidies Agreement. In two separate challenges in 1979 and 1980 to the sugar export subsidy programme of the European Communities by Australia and Brazil, panels were unable to find that the export refunds provided by the Communities resulted in a "more than equitable share" of world export trade.⁶² Similarly, in the 1983 US challenge to export subsidies on wheat flour by the European Communities (quoted in the US further submission), "[t]he [p]anel found that it was unable to conclude as to whether the increased [EC] share [of world exports of wheat flour] has resulted in the EEC 'having more than an equitable share' in terms of Article 10 [of the Subsidies Code], in light of the highly artificial levels and conditions of trade in wheat flour, the complexity of developments in the markets, including the interplay of a number of special factors, the relative importance of which it was impossible to assess, and, most importantly, the difficulties inherent in the concept of 'more than equitable share'".⁶³

130. Significantly, the latter two of these panel reports explicitly considered the 1979 Tokyo Round Subsidies Code and its interpretive gloss on the "more than equitable share language". Article 10.2 of the 1979 Subsidies Code (of which both Brazil and the United States were signatories) stated, in pertinent part:

For purposes of Article XVI:3 of the General Agreement and paragraph 1 above:

- (a) "more than an equitable share of world export trade" shall include any case in which the effect of an export subsidy granted by a signatory is to displace the exports of another signatory bearing in mind the developments on world markets;
- (b) with regard to new markets traditional patterns of supply of the product concerned to the world market, region or country, in which the new market is situated shall be taken into account in determining 'equitable share of world export trade' [.]

That is, the 1979 Subsidies Code represented an effort to make operational the discipline provided in GATT 1994 Article XVI:3 by giving additional meaning to the phrase "more than an equitable share of world export trade". Despite that effort, however, the panel considering the Brazilian challenge to EC sugar export subsidies and the panel considering the US challenge to EC wheat flour export subsidies remained unable to find any inconsistency with GATT 1994 Article XVI:3 (in the words of

⁶² *European Communities – Refunds on Exports of Sugar*, L/4833, 26S/290 (adopted 6 November 1979) (complaint by Australia); *European Communities – Refunds on Exports of Sugar*, L/5011, 27S/69 (adopted 10 November 1980).

⁶³ *European Economic Community – Subsidies on Export of Wheat Flour*, SCM/42, para. 5.3 (unadopted 21 March 1983).

the Wheat Flour panel) “in light of . . . , most importantly, the difficulties inherent in the concept of ‘more than equitable share’”.

131. Thus, there was a recognition in the Uruguay Round subsidies negotiations that the effort in the 1979 Subsidies Code to make GATT 1994 Article XVI:3 more operationally effective had not succeeded. For example, a reference paper on GATT subsidies rules and the existing status of discussion of these rules prepared by the GATT Secretariat for the Negotiating Group on Subsidies and Countervailing Measures states:

The most pronounced difficulties have occurred in connection with the concept of “more than an equitable share” embodied in Article XVI:3 of the GATT. The Agreement on Subsidies and Countervailing Measures (Article 10) attempted to bring precision to Article XVI:3 but it has not always been found to give clear guidance on its interpretation. Consequently a number of disputes involving the concept of “more than an equitable share” have not found a satisfactory solution and in some cases have provoked retaliatory subsidization. The case-by-case application of this concept has revealed its imprecisions and the fact that it largely refers to notions which escape objective criteria. There is, for example, sufficient imprecision in this concept to allow countries using export subsidies to argue that these subsidies do not result in obtaining more than equitable share. On the other hand it is not always possible to provide causality between the subsidy and the increase share. Furthermore, it is impossible to derive a general line of case law from the decisions of panels, some of which have given divergent interpretations.⁶⁴

132. A checklist of issues for the negotiations based on Contracting Parties’ written submissions and oral statements prepared by the Secretariat demonstrates that Contracting Parties were well aware of these difficulties and the need to move away from the “more than an equitable share” concept:

There is a need for review, with a view to improving GATT disciplines, of the provisions of Article XVI:2 and 3. Notably there is a need to build on the recognition embodied in Article XVI:2 and the exhortation in the first sentence of XVI:3 in the direction of improving the conditions of competition on world markets for primary products currently covered by the equitable share criterion in the second sentence of Article XVI:3.

The review should examine the application of the “more than an equitable share” rule for primary products. This rule has serious conceptual flaws and in practice has failed to provide clear guidance as to the permissible scope of primary product subsidization. . . .

The Negotiating Group should consider negotiating a similar prohibition to that of Article 9 of the Code on the use of export subsidies for forest, fishery and farm products.

The prohibition on export subsidies for products other than basic or primary products under Article XVI:4 and Article 9 of the Code should be extended to agricultural, forestry and fishery products, in other words to all basic or primary products.

A major objective of these negotiations should be to extend the existing prohibition on export subsidies to cover all products, primary as well as non-primary.

⁶⁴ *Subsidies and Countervailing Measures: Note by the Secretariat*, MTN.GNG/NG10/W/4, at 79 (28 April 1987) (Section VI.3).

There are serious deficiencies in Article XVI:3 of the GATT and in Article 10 of the Code, notably the fundamental problems connected with the 'more than equitable share' concept. However, these problems arise from the basic fact that current disciplines for primary products are significantly weaker than those which apply to manufactured goods. They cannot be resolved merely by making minor adjustments to rules which are intrinsically defective. The only genuine, long-term solution is an effective prohibition on all export subsidies. Accordingly at this stage of the negotiating process, there is little value in trying to improve the "more than equitable share" rule, which is only relevant so long as there is no general prohibition on export subsidies.⁶⁵

133. Reflecting the desire of Members to move away from the "more than an equitable share" concept which had repeatedly been found by panels to be incapable of application, the WTO Subsidies Agreement does not provide any further definition or interpretation of GATT 1994 Article XVI:3. Instead, it contains the general prohibition on export subsidies in Article 3 and rules on adverse effects, including serious prejudice.

M. THREAT CLAIMS

187. Please provide USDA's projections of marketing loan/LDP payments, direct payments and counter-cyclical payments to be made during MY2003 through 2007 based on the most recent USDA baseline projection. US

134. The following table shows projections for cotton marketing loan/LDP payments, direct payment and counter-cyclical payments for crop years 2003 through 2008, as published in the FY2004 Mid-Session Review on 15 July 2003. We note that projected outlays for marketing year 2003 are likely to be significantly overstated given the increase in prices and futures prices over the course of this marketing year. For example, no marketing loan payments are currently being made because the adjusted world price is above the marketing loan rate.

Projected outlays (million dollars)

Item	2003	2004	2005	2006	2007	2008
Direct payments	587	587	587	587	587	587
Counter-cyclical payments	929	602	521	521	521	521
Loan deficiency payments	420	298	193	137	137	82
Marketing loan gains	22	13	8	6	6	3
Certificate gains 1/	196	114	75	55	52	29

1/ Includes value of non-cash marketing loan transactions.

188. Can the United States comment on the FAPRI projections for cotton provided in Exhibit BRA-202? US

135. The FAPRI projections presented by Brazil in Exhibit BRA-203 reflect the January 2003 FAPRI projections. These projections were published by Iowa State University in January 2003.⁶⁶ The same projections were published by FAPRI at the University of Missouri in March 2003 and were referenced by the United States in Exhibit US-52.

⁶⁵ *Checklist of Issues for Negotiations: Note by the Secretariat*, MTN.GNG/NG10/W/9/Rev.4, at 26-28 (12 December 1988).

⁶⁶ Food and Agricultural Policy Research Institute. *FAPRI 2003: US and World Agricultural Outlook*. Iowa State University Staff Report 1-03. January 2003.

136. Of significance is the difference between the January 2003 baseline and the preliminary baseline of November 2002 utilized by Dr. Sumner in his analysis. Under the January 2003 baseline, the Adjusted World Price (AWP) forecasts for 2002/03 to 2007/08 are considerably higher than the forecasts made in the preliminary November 2002 baseline. Because loan deficiency payments and marketing loan gains are calculated based on the difference between the loan rate and the AWP, this means that expected marketing loan subsidies under the November 2002 baseline are far higher than expected marketing loan subsidies under the January 2003 baseline. Thus, the effects of eliminating marketing loans would tend to be biased upwards using the preliminary November 2002 baseline.

Differences in the Adjusted World Price forecast between the November 2002 and January 2003 FAPRI baseline (\$/lb)

	2002/03	2003/04	2004/05	2005/06	2006/07	2007/08
November 2002 baseline 1/	0.3597	0.3722	0.3983	0.4194	0.436	0.4548
January 2003 baseline 2/	0.448	0.454	0.46	0.46	0.467	0.48
Difference	0.0883	0.0818	0.0617	0.0406	0.031	0.0252

1/ As presented by Dr. Sumner in Annex I and oral statement of 7 October 2003.

2/ As reported in Exhibit BRA-203 and Exhibit US-52

N. CLARIFICATIONS

189. Please indicate whether the correct figure in paragraph 37 of Brazil's 7 October oral statement is 38.1% or 38.3%? BRA

190. Please confirm that the figure "17.5" in paragraph 43 of Brazil's 7 October oral statement, is "percentage point". BRA

191. Could Brazil clarify its statement in para. 12 of its 9 September further submission: "Alternatively crop insurance is not specific because the 2000 ARP Act denies benefits to commodities representing more than half of the value of US agriculture. Further US crops represent only 0.8 per cent of total US GDP." (emphasis added) BRA

List of Exhibits

- 64 Lin, W., et al.. Supply Response Under the 1996 Farm Act and Implications for the US Field Crops Sector. US Department of Agriculture, Economic Research Service, Technical Bulletin No. 1888, Appendix table 21
- 65 Amount and percentage of upland cotton acreage coverage by crop insurance policy
- 66 Premiums paid by upland cotton producers
- 67 Insurance indemnity payments to upland cotton producers
- 68 New York Cotton Futures, Average Daily Closing Prices for December 2003 Contract (chart and data)
- 69 US Department of Agriculture, Economic Research Service, Cost of Production Estimates; Commodity-Weighted Exchange Rate Estimates
- 70 US and Rest of World Exports of Upland Cotton, Year-Over-Year Per cent Change, 1996-2002
- 71 US Exports and Domestic Consumption of Upland Cotton, 1996-2002
- 72 US Department of Agriculture, Press Release on Adjusted World Price (18 October 2003)
- 73 Weekly Price Movements: Adjusted World Price, Liverpool A-Index, New York cotton futures, spot market price, January 1996 to present
- 74 National Agricultural Statistics Service, Planted Acreage of Selected Crops by Region and State