EUROPEAN COMMUNITIES – EXPORT SUBSIDIES
ON SUGAR

COMPLAINT BY AUSTRALIA

Report of the Panel
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I. INTRODUCTION

1.1 This proceeding was initiated by three complaining parties, Australia, Brazil and Thailand.

1.2 In communications dated 27 September 2002, Australia and Brazil requested consultations with the European Communities pursuant to Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"), Article XXII:1 of the General Agreement on Tariffs and Trade 1994 ("GATT 1994"), Article 19 of the Agreement on Agriculture, and Articles 4.1 and 30 of the Agreement on Subsidies and Countervailing Measures ("SCM Agreement"), with respect to export subsidies provided by the European Communities to its sugar industry. Australia and Brazil held consultations with the European Communities in Geneva on 21 and 22 November 2002 but these consultations did not result in a resolution of the dispute.

1.3 On 14 March 2003, pursuant to Article 4 of the DSU, Article XXIII of the GATT 1994, Article 19 of the Agreement on Agriculture, and Articles 4 and 30 of the SCM Agreement, Thailand requested consultations with the European Communities with respect to certain subsidies provided by the European Communities in the sugar sector. Consultations were held in Geneva on 8 April 2003 but failed to resolve the dispute.

1.4 On 21 July 2003, Australia, Brazil and Thailand requested the establishment of a panel pursuant to Articles 4.7 and 6 of the DSU and Article XXIII:2 of the GATT 1994.

1.5 At its meeting on 29 August 2003, the Dispute Settlement Body (DSB) established a panel pursuant to the requests of Australia (WT/DS265/21); Brazil (WT/DS266/21); and Thailand (WT/DS283/2), in accordance with Article 6 of the DSU. At that meeting, the parties to the dispute agreed to establish a single panel pursuant to Article 9.1 of the DSU with standard terms of reference.

1.6 The terms of reference are the following:

"To examine, in the light of the relevant provisions of the covered agreements cited by Australia in document WT/DS265/21, by Brazil in document WT/DS266/21 and by Thailand in document WT/DS283/2, the matters referred therein to the DSB by Australia, Brazil and Thailand, and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements."

2. Panel composition

1.7 On 15 December 2003, Australia, Brazil and Thailand requested the Director-General to determine the composition of the panel, pursuant to paragraph 7 of Article 8 of the DSU. This paragraph provides:

"If there is no agreement on the panellists within 20 days after the date of the establishment of a panel, at the request of either party, the Director-General, in consultation with the Chairman of the DSB and the Chairman of the relevant Council or Committee, shall determine the composition of the panel by appointing the panellists whom the Director-General considers most appropriate in accordance with

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1 WT/DS265/1, G/L/569, G/AG/GEN/52, G/SCM/D47/1 and WT/DS266/1, G/L/570, G/AG/GEN/53, G/SCM/D48/1, respectively.
2 WT/DS283/1, G/L/613, G/AG/GEN/58, G/SCM/D53/1.
any relevant special or additional rules or procedures of the covered agreement or
covered agreements which are at issue in the dispute, after consulting with the parties
to the dispute. The Chairman of the DSB shall inform the Members of the
composition of the panel thus formed no later than 10 days after the date the
Chairman receives such a request."

1.8 On 23 December 2003, the Director-General accordingly composed the Panel as follows:

Chairman: Mr Warren Lavorel

Members: Mr Gonzalo Biggs
          Mr Naoshi Hirose

3. Third parties

1.9 Australia, Barbados, Belize, Brazil, Canada, China, Colombia, Côte d’Ivoire, Cuba, Fiji,
Guyana, India, Jamaica, Kenya, Madagascar, Malawi, Mauritius, New Zealand, Paraguay, Saint Kitts
and Nevis, Swaziland, Tanzania, Thailand, Trinidad and Tobago, and the United States notified their
interest to participate in the panel proceedings as third parties.

1.10 At the request of some third parties, all third parties were invited to attend, as observers, the
entirety of the first and second substantive meetings with the parties (see paragraphs 2.5-2.9 below).

4. Organizational meeting

1.11 On 9 January 2004, the Panel sent a draft timetable and draft working procedures to the
parties. These were subsequently discussed at the organizational meeting that the Panel held with the
parties on 14 January 2004. The timetable (tentative) and working procedures were adopted as
amended at the organizational meeting. No decision with respect to third parties was taken at the
organizational meeting. (See also paragraphs 2.1-2.9 below.)

5. Meetings with the parties and third parties

1.12 The Panel met with the parties on 30, 31 March, 1 April, and on 11 and 12 May, 2004. In
accordance with paragraph 6 of Appendix 3 of the DSU, third parties were invited to a session during
the first substantive meeting set aside for that purpose. Third parties were also invited to observe the
entirety of the first and second substantive meetings (see paragraphs 2.5-2.9 below).

6. Reports

1.13 At the request of the European Communities, pursuant to Article 9.2 of the DSU on multiple
complaints, the Panel is issuing three reports for this dispute, one for each complaining party.

1.14 On 4 August 2004, the Panel issued its Interim Reports to the parties. On 17 August 2004,
the Panel received comments from the parties. On 24 August 2004, the parties submitted further
written comments on the comments received on 17 August 2004. The Panel issued its Final Reports
to the parties on 8 September 2004.
II. PRELIMINARY RULINGS BY THE PANEL AND OTHER ISSUES

1. Notification of third parties’ interest

2.1 In this case, the Republic of Kenya (Kenya) on 26 September, 2003 and the Republic of Côte d’Ivoire (Côte d'Ivoire) on 5 November, 2003 requested to participate as third parties after the ten-day notification period specified by the Chairman of the DSB at the time of the establishment of the Panel, but before the Director-General was asked by the parties to compose the Panel pursuant to Article 8.7 of the DSU. The parties agreed to accept Kenya as a third party but the Complainants objected to the participation of Côte d'Ivoire.

2.2 Article 10 of the DSU is silent on when Members need to notify to the DSB their interest in participating in any specific dispute as third parties. All parties referred to the GATT Council Chairman's Statement of June 1994, providing for a ten-day notification period. The status of that Chairman's Statement had been discussed on several occasions at the DSB and the timing of third-party notifications was the subject of proposals in the context of the DSU negotiations.

2.3 The Panel recalled, inter alia, the Appellate Body's decision in EC – Hormones, which stated that "the DSU leaves panels a margin of discretion to deal, always in accordance with due process, with specific situations that may arise in a particular case and that are not explicitly regulated." In addition, with regard to the two requests at issue, the Panel noted that in this particular dispute:

(a) the selection and composition of the Panel did not appear to have been adversely affected; and

(b) the Panel process had not been hampered.

2.4 On the basis of these considerations, the Panel therefore decided, in its ruling dated 16 January 2004, to accept as third parties all Members that had expressed a third-party interest and saw no reason to treat them differently. In doing so, the Panel emphasized that its decision was specific to this dispute and was not intended to offer a legal interpretation of the ten-day notification period referred to in the GATT Council Chairman's Statement.

2. Third parties enhanced rights

2.5 Prior to the Panel starting work, Mauritius, on behalf of 14 ACP sugar producing countries, requested that the Panel provide the ACP countries with extended third-party rights in the proceedings of the Panel. At the preliminary stage of the dispute, i.e. before any submissions had been made to the Panel, the Panel was not in a position to assess whether the economic situation of any third party would be specifically affected by the outcome of this dispute. However, in light of the importance of trade in sugar for many third parties, the Panel decided, in a ruling dated 16 January 2004, as follows:

"After hearing the parties' views and considering the third parties' written communications on this issue, the Panel invited all third parties to attend the entirety of the first substantive meeting as observers; to make a written submission to the Panel and receive the submissions of the parties and third parties for that meeting; and to present their views orally at a session of that meeting, set aside for that purpose."

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3 GATT Council C/COM/3.
5 Barbados, Belize, Côte d'Ivoire, Fiji, Guyana, Jamaica, Kenya, Madagascar, Malawi, Mauritius, St. Kitts and Nevis, Swaziland, Tanzania and Trinidad and Tobago.
2.6 In a letter dated 1 April 2004, the same countries requested enhanced rights as third parties in the remaining procedure of the Panel. After comments by the parties on this request, the Panel decided, in a ruling dated 14 April 2004 "that, beyond those rights already provided for in the DSU, in the Working Procedures adopted by this Panel, as well as in its ruling dated 16 January 2004 (see paragraph 2.4 above), the following additional rights were granted to all third parties for the purpose of this case:

(a) the third parties will receive a copy of the written questions to the parties posed in the context of the first substantive meeting of the Panel;

(b) the third parties will receive the written rebuttals of the parties to the second meeting of the Panel and the parties' replies to the questions mentioned in (i) above;

(c) the third parties may attend the second substantive meeting of the Panel to take place on 11 and 12 May 2004, as observers (but it is not envisaged that the third parties will provide any further written submission or make an oral statement to the Panel during that second meeting); and

(d) the third parties will review the summary of their respective arguments in the draft descriptive part of the Panel report."

2.7 In considering whether to grant any additional rights to third parties, the Panel believed that it was important to guard against an inappropriate blurring of the distinction drawn in the DSU between the rights of parties and those of third parties. Furthermore, the Panel considered that, as a matter of due process, it was appropriate to provide the same procedural rights to all third parties."

2.8 On behalf of the sugar-exporting ACP countries, Guyana, on 22 April 2004, requested that ACP sugar-producing countries be allowed to "present arguments, including oral statements and observations " at the second substantive meeting of the Panel with the parties.

2.9 After consideration of Guyana’s request on behalf of ACP sugar-producing countries, the Panel did not see any need to change its decision of 14 April 2004 (see paragraphs 2.6 and 2.7 above) and reiterated its invitation to all third parties to attend the second meeting of the Panel as "observers," on the understanding that the third parties would not make any (further) written or oral statements to the Panel.

3. Request for additional working procedures for the protection of proprietary information

2.10 On 13 January 2004, Australia and Thailand requested that the Panel adopt additional working procedures for the protection of proprietary information purchased from LMC International (LMC) relating to data on EC costs of sugar production that the complaining parties claimed they would use in their first written submission. Such additional working procedures would, inter alia, limit the third parties' access to such confidential information to "view-only" prescriptions.

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6 On this question, Australia and Thailand jointly sent a written communication to the Panel on 13 January 2004 and Australia, with the support of Thailand, sent another written communication to the Panel on 19 January 2004. Finally, Australia, Brazil and Thailand also sent a written communication to the Panel on 23 January 2004.
2.11 The European Communities opposed\(^7\) the request, arguing, *inter alia*, that LMC statistical data was not the type of information that should benefit from exceptional and additional rules for the protection of confidential information. It added that the rules suggested by Australia and Thailand were discriminatory *vis-à-vis* third parties who would only be entitled to "view" the confidential data.

2.12 After consideration of the parties’ arguments, the Panel decided, in a ruling dated 27 January 2004, to reject the request from Australia and Thailand.

2.13 The Panel recalled, in particular, that the following provisions of the *DSU* and of the Rules of Conduct, were relevant and applicable to the issue of confidential information in WTO dispute settlement proceedings.

2.14 Article 18.2 of the *DSU* on communications with panels or the Appellate Body provides:

"2. Written submissions to the panel or the Appellate Body shall be treated as confidential, but shall be made available to the parties to the dispute. Nothing in this Understanding shall preclude a party to a dispute from disclosing statements of its own positions to the public. *Members shall treat as confidential information submitted by another Member to the panel or the Appellate Body which that Member has designated as confidential.* A party to a dispute shall also, upon request of a Member, provide a non-confidential summary of the information contained in its written submissions that could be disclosed to the public." (emphasis added)

Moreover, paragraph 3 of Appendix 3 to the *DSU* states:

"3. The deliberations of the panel and the *documents submitted to it shall be kept confidential*. Nothing in this Understanding shall preclude a party to a dispute from disclosing statements of its own positions to the public. *Members shall treat as confidential information submitted by another Member to the panel which that Member has designated as confidential.* Where a party to a dispute submits a confidential version of its written submissions to the panel, it shall also, upon request of a Member, provide a non-confidential summary of the information contained in its submissions that could be disclosed to the public." (emphasis added)

2.15 The Panel further ruled that "All parties and third parties would thus have to treat as confidential any information identified by a party to this dispute as confidential (including the statistical data from LMC if Australia and Thailand had designated them as such). The parties and third parties shall not disclose any such information without the formal authorization of the party who had designated such information as confidential. In this regard, parties and third parties have the responsibility for all members of their delegation. In particular, no member of the delegation of any party or third party shall disclose to any person outside the delegation any information designated as confidential by a party to the present dispute. Any such information could only be used for the purposes of submissions and argumentation in this dispute."

2.16 The Panel noted also that it had the right not only to receive confidential information, but also to seek it. To this effect, Article 13 of the *DSU* on the Right to Seek Information provides that:

"1. Each panel shall have the right to seek information and technical advice from any individual or body which it deems appropriate. However, before a panel seeks such

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\(^7\) The Panel received written communications from the European Communities on 3 January 2004 and 15 January 2004. Although not solicited, the Panel also received written communications from three third parties: Fiji on 16 January 2004; Mauritius on 16 January 2004; and Jamaica on 20 January 2004.
information or advice from any individual or body within the jurisdiction of a Member it shall inform the authorities of that Member. A Member should respond promptly and fully to any request by a panel for such information as the panel considers necessary and appropriate. Confidential information which is provided shall not be revealed without formal authorization from the individual, body, or authorities of the Member providing the information." (emphasis added)

2.17 The Panel was of the view that parties and third parties were bound by the DSU provisions on confidentiality. In the present circumstances, these provisions were, according to the Panel, sufficient to protect the confidentiality of the statistical data from LMC, during the panel process and afterwards, as indicated above.

2.18 As for the Panel, pursuant to the DSU and the Rules of Conduct, it was bound not to disclose, in the panel reports, or in any other way, any information designated as confidential by a party under these procedures.

2.19 Finally, the Panel recalled that it had the right to reconsider the need for additional working procedures for the protection of confidential information if circumstances changed and so warranted such exceptional working procedures after consultation with the parties.

4. Amicus curiae

2.20 On 24 May 2004, the Panel received an unsolicited amicus curiae brief from Wirtschaftliche Vereinigung Zucker ("WVZ"), an association representing German sugar producers. The Panel invited the parties to make comments thereon, if they so wished. Australia, Brazil and Thailand requested in their comments that the Panel reject the document submitted by WVZ on the grounds, inter alia, of due process as well as the late submission of the document. The European Communities did not wish to make any comments on the WVZ document.

5. Breach of confidentiality

2.21 Brazil informed the Panel on 2 June 2004 that the amicus curiae brief submitted by WVZ disclosed information that Brazil had submitted to the Panel in confidence. Brazil, accordingly, wished to bring this breach of confidentiality to the Panel's attention, and requested that the Panel "investigate how the breach occurred". Thailand supported the request made by Brazil in this regard.

2.22 The Panel noted the seriousness of the matter at issue, and invited the parties and third parties to comment on Brazil's allegation, and on the appropriate remedy, "if such a breach had in fact occurred." Such comments were to be submitted by the end of the day on 8 June 2004.

2.23 The European Communities noted that it attached the utmost importance to the strict observance of the confidentiality rules set out in the DSU and in the working procedures of the Panel by all parties and third parties. It shared the concerns expressed by Brazil. It noted further that it had treated as strictly confidential all information designated as such by Brazil in these proceedings.

2.24 On 4 June 2004, the Panel invited, by letter, comments from the parties and third parties "on Brazil's allegation, and on the appropriate remedy, if such a breach has in fact occurred."

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8 With regard to the obligation of the Panel (and members of the Secretariat) to respect confidentiality, Articles III:2, IV:1 and VII:1 of the Rules of Conduct for the Settlement of Disputes confirm that members of the Panel and Secretariat staff assisting the Panel shall at all times maintain the confidentiality of dispute settlement deliberations and proceedings together with any information identified by a party as confidential. No covered person shall at any time use such information acquired during such deliberations and proceedings to gain personal advantage or advantage for others.
2.25 The Panel received responses, dated 8 June 2004, from Australia, the European Communities (parties), and from India (third party). All three Members supported the request made by Brazil (see paragraph 2.21 above).

2.26 On 10 June 2004, the Panel requested, in a letter, information from the WVZ "with respect to the exact source[s] (documents, websites, etc.) used for the data referred to" in its document. The Panel further requested "information about the original currency nominations if different from the nominations in Euros used" in the document.

2.27 The Panel received a response from WVZ on 15 June 2004 in which WVZ indicated that it had been able to examine an attachment to Brazil's submission, the Datagro report, which referred to another LMC study than the one used by WVZ in the document received by the Panel on 24 May 2004. According to WVZ, this LMC document was not designated as confidential. It also indicated that WVZ was "not in a position to reveal the source of its information regarding the evidence submitted by Brazil."

2.28 Comments on the response from WVZ were received from Brazil on 18 June 2004 in which Brazil reiterated its request (see paragraph 2.21) that the Panel summarily reject the WVZ amicus curiae brief. Brazil also requested that the Panel "make a full report of this incident to the Dispute Settlement Body."

III. FACTUAL ASPECTS

3.1 The European Communities established, in 1968, a Common Organization (CMO) for Sugar, the main rules of which are today set out in "Council Regulation (EC) No. 1260/2001 on the common organization of the markets in the sugar sector" (the Regulation), dated 19 June 2001. The Regulation is valid for marketing years 2001/2002 to 2005/2006 and the information below refers to those years.

3.2 The Regulation sets out the basic rules with respect to, inter alia, the intervention prices for raw and white sugar, respectively; the basic price and the minimum price for beet; A and B quotas as well as C sugar; import and export licences; levies; export refunds; and preferential import arrangements.

1. Product coverage

3.3 The EC sugar regime applies inter alia to cane and beet sugar, sugar beet, and sugar cane as well as to isoglucose.9 The sugar cane and the sugar beet are primarily transformed into raw sugar and/or white sugar.

2. Quotas

3.4 The sugar regime establishes two categories of production quotas: one for A sugar and the other one for B sugar (see paragraph 3.6). These quotas constitute the maximum quantities eligible for domestic price support and direct export subsidies (in EC terminology, "refunds"). The quota system does not involve any limits on the quantities of sugar that may be produced or exported. However, sugar produced in excess of A and B quantities, called C sugar, while not subject to quota, is not eligible for domestic price support or direct export subsidies and must be exported.10 If no

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9 Article 1 of the Regulation.
10 Article 10.5 of the Regulation.
proof has been supplied that the C sugar has been exported within the required time limits, a charge is levied on that sugar.\footnote{Article 13 of the Regulation.}

3.5 Sugar production quotas are allocated in the first instance to member States, with current quotas applying to the marketing years 2001/02 to 2005/06. Member States, in turn, allocate quota to each undertaking (processor) on the basis of its actual production during a particular reference period.\footnote{Paragraph 11 of the Recital of the Regulation.}

3.6 The Regulation fixes a basic quota for the entire Community for the production of A and B sugar. The basic quantities for A and B sugar are set, respectively, at 11,894,223.3 tonnes (white sugar)\footnote{Article 11.1 of the Regulation.} and 2,587,919.20 tonnes (white sugar)\footnote{Article 11.2 of the Regulation.}. Each of these quantities is broken down by member State which in turn allocates quantities to producer undertakings established on its territory. A Member state may transfer quota between undertakings, “taking into consideration the interests of each of the parties concerned, particularly sugar beet and cane producers”, up to a maximum of 10 per cent of an undertaking’s A or B quota (with some limited exceptions).\footnote{Article 12 of the Regulation.} Each undertaking may carry forward to the next marketing year sugar that it has produced in excess of its A and B quota (i.e. C sugar) up to a limit of 20 per cent of its A quota.\footnote{Commission Regulation (EEC) No. 65/82, Article 2.} It may also carry forward all or part of its B sugar production. In addition, an undertaking may carry forward all or part of its production of A and B sugar which has been reclassified as C sugar after reduction of the guaranteed quantities in conformity with Article 10 of the Regulation. Quantities carried forward must be stored for 12 consecutive months from a date to be determined.\footnote{Article 14 of the Regulation.}

3. Intervent ion price

3.7 To achieve the objectives of the common agricultural policy and in order to stabilize the EC sugar market, the EC Regulation provides for intervention agencies to buy in sugar. An intervention price is established for this purpose at a level which will ensure a fair income for sugar-beet and sugar-cane producers.\footnote{Recital 2 of the Regulation.} The intervention price valid for standard quality\footnote{“Such standard qualities should be average qualities representative of sugar produced in the Community and should be determined on the basis of criteria used by the sugar trade.” Recital, 3 of the Regulation.} is €63.19/100 kg for white sugar and €52.37/100 kg for raw sugar.\footnote{Article 2 of the Regulation.} The actual price received for white sugar is, on average, around 10 to 20 per cent in excess of the intervention price. The intervention price is valid for the domestic market and as a guaranteed minimum price to be paid by EC purchasers for imports of sugar from ACP states and India.

4. Basic and minimum prices

3.8 A basic price for quota beet of standard quality\footnote{For the definition of "standard quality" of beet, see Annex II of the Regulation.} is derived from the intervention price of white sugar and has been established at €47.67 per tonne.\footnote{Article 3 of the Regulation.} The Regulation also establishes minimum prices for A and B beet, standard quality, intended to be processed into A and B sugar, respectively and paid by sugar manufacturers buying beet. The minimum price of A beet has been set at €46.72
per tonne whereas the minimum price for B beet has been fixed at €32.42 per tonne.\textsuperscript{23} Manufacturers are required to pay growers at least the minimum price for A and B beet they process into A and B sugar. The price for beet paid by the manufacturer to produce C sugar may be lower than that paid for A and B beet.\textsuperscript{24}

5. Basic production levy and B levy

3.9 In accordance with Article 15, a basic production levy shall be charged to manufacturers on their production of \textit{inter alia} A and B sugar, when the forecasts and adjustments\textsuperscript{25} result in a foreseeable overall loss.\textsuperscript{26} Such a levy shall not exceed 2\% per cent of the intervention price for white sugar. Another levy of a maximum 37.5\% per cent of the intervention price for B sugar may be charged if the loss is not fully covered by the proceeds from the levy mentioned above.

6. Import and export licences

3.10 Imports into and exports from the European Communities of \textit{inter alia} cane or beet sugar and isoglucose are subject to the presentation of an import or export licence, issued by the respective member States. These licences are valid throughout the Community and are subject to the lodging of a security.

7. Export refunds

3.11 In order to enable \textit{inter alia} the products mentioned in paragraph 3.3 above to be exported without further processing at world market prices, the difference between the world market price and the Community price may be covered by export refunds. The export refund for raw sugar may not exceed that of white sugar. Such refunds shall be the same for the whole Community and for all sugar except C sugar but may vary according to destination. Refunds may be fixed at regular intervals or by a tendering procedure for products for which such a procedure has been used in the past.\textsuperscript{27} Refunds are paid directly from the EC budget. However, the system of levies outlined in paragraph 3.9 is designed to recover from EC producers part of the cost of export refunds for quota sugar produced in excess of EC consumption.

8. Management Committee for Sugar

3.12 Article 42 of the Regulation establishes a Management Committee for Sugar to assist the EC Commission to consider any issue referred to it by the Commission, or by a member State, with respect to the management of the sugar regime, such as the preparation of supply and demand forecasts.

9. Commitments

3.13 The commitments set out in the table in Section II, of Part IV of the EC's Schedule amount to €499.1 million and 1,273.5 thousand tonnes. A footnote to the table provides:

"Does not include exports of sugar of ACP and Indian origin on which the Community is not making any reduction commitments. The average of export in the period 1986 to 1990 amounted to 1.6 mio t."

\textsuperscript{23} Article 4 and Article 5 of the Regulation.  
\textsuperscript{24} Article 21 of the Regulation.  
\textsuperscript{25} Paras. 1 and 2 of Article 15 of the Regulation.  
\textsuperscript{26} See paragraph 3 of Article 15 of the Regulation.  
\textsuperscript{27} Article 27 of the Regulation.
According to the European Communities’ latest notification (marketing year 2001/2002) to the Committee on Agriculture, total exports of sugar amounted to 4.097 million tonnes (product weight).

10. Preferential import arrangements

3.14 The European Communities is required to import 1,294,700 tonnes (white sugar equivalent) of cane sugar, called "preferential sugar" under Protocol 3 to Annex IV to the ACP/EC Partnership Agreement.\(^{28}\) It also has agreed to import 10,000 tonnes of preferential sugar from India. Preferential sugar is imported at zero duty and at guaranteed prices.\(^{29}\)

3.15 In addition to imports of ACP/India preferential cane sugar, special preferential raw cane sugar (SPS sugar) may be imported from the same countries which benefit from the ACP/India preferential arrangements in order to ensure adequate supplies to Community refineries.\(^{30}\) Volumes of SPS sugar vary from year to year but have amounted to around 320,000 tonnes per year in recent years. A reduced rate of duty is levied on imports of such sugar. The quantities of SPS sugar to be imported is decided on the basis of a supply balance forecast for each marketing year.

11. Review

3.16 The current EC sugar regime is scheduled for review in 2006.

IV. MAIN ARGUMENTS\(^{31}\)

A. PARTIES’ REQUESTS FOR FINDINGS

4.1 The complaint examined by the Panel is related to the European Communities' measures with respect to the common organization of its markets in sugar.

4.2 Australia requests, for the reasons set out in its submission, that the Panel make the following rulings:

- C sugar produced under the EC regime is provided with an export subsidy within the meaning of Article 9.1(c) of the Agreement on Agriculture;

- this export subsidy has not been subjected to the EC's reduction commitments under the Agreement on Agriculture, inconsistently with the provisions of Article 9.1 of that Agreement;

- as C sugar exports – which are provided with export subsidies defined under Article 9.1(c) – are in excess of the quantity outlay commitment levels specified in Section II of Part IV of the EC Schedule, the EC is acting inconsistently with the provisions of Article 3.3 of the Agreement on Agriculture;

\(^{28}\) As referred to in Chapter 2 of Title II of the Regulation.

\(^{29}\) Commission Regulation (EC) No. 1159/2003 sets out detailed rules of application for the importation of cane sugar under certain tariff quotas and preferential arrangements.

\(^{30}\) Article 39 of the Regulation.

\(^{31}\) Note by the Panel: Note that this section summarizes the parties arguments and evidence as the Panel understood them. Note also that the individual factual and legal arguments by each of the complaining parties were endorsed by the other complaining parties. Note finally that footnotes in this and the section that summarizes the arguments of third parties are those of the parties if not indicated otherwise.
• alternatively, if the Panel finds that the EC's export subsidies on C sugar are not export subsidies within the meaning of Article 9.1 of the Agreement on Agriculture, the EC is applying other export subsidies in a manner which results in, or threatens to lead to, circumvention of export subsidy commitments, inconsistently with the provisions of Article 10.1 of the Agreement on Agriculture;

• under either of the alternatives, as the EC provides export subsidies on C sugar otherwise than in conformity with the Agreement on Agriculture and with the commitments as specified in its Schedule, the EC is acting inconsistently with its undertaking under the provisions of Article 8 of the Agreement on Agriculture;

• the EC is providing export subsidies to C sugar inconsistently with the provisions of Articles 3.1(a) and 3.2 of the SCM Agreement;

• the EC grants direct export subsidies on the export of 'ACP/India equivalent' sugar, within the meaning of Article 9.1(a) of the Agreement on Agriculture;

• the export subsidies have not been subjected to the EC's reduction commitments under the Agreement on Agriculture, inconsistently with Article 9.1;

• the footnote to the EC's Schedule does not permit the EC to derogate from its reduction commitment obligations under Articles 9.1, 3.3 and 8 of the Agreement on Agriculture;

• the export subsidies on 'ACP/India equivalent' sugar are in excess of the budgetary outlay and quantity reduction commitments specified in the EC's Schedule, inconsistently with Article 3.3 of the Agreement on Agriculture;

• as the EC is providing export subsidies on 'ACP/India equivalent' sugar otherwise than in conformity with the Agreement on Agriculture and with the commitments specified in its Schedule, it is acting inconsistently with the provisions of Article 8 of the Agreement on Agriculture;

• the EC is providing direct export subsidies to 'ACP/India equivalent' sugar, within the meaning of paragraph (a) of Annex I of the SCM Agreement, inconsistently with the provisions of Article 3.1(a) of that Agreement.

4.3 Australia requests that the Panel recommend to the Dispute Settlement Body, in accordance with Article 19.1 of the Understanding on Rules and Procedures Governing the Settlement of Disputes and Article 4.7 of the Subsidies Agreement, that the EC:

• bring its export subsidies for sugar into conformity with its obligations under the Agreement on Agriculture; and

• withdraw the export subsidies inconsistent with the SCM Agreement within 90 days.

4.4 Brazil requests, for the reasons set out in its submission, that the Panel make the following rulings:

• the EC violates Article 9.1(a) of the Agreement on Agriculture since it does not subject to its reduction commitments all of the sugar to which it grants direct export subsidies;
• the EC accords subsidies within the meaning of Article 9.1(c) of the *Agreement on Agriculture* to its exports of C sugar; the EC therefore grants subsidies in excess of its quantity reduction commitment for sugar inconsistently with Articles 3.3 and 8 of the *Agreement on Agriculture*;

• the export subsidies that the EC grants to A and B quota sugar and to ACP/India sugar are subject to the EC's reduction commitments for sugar; the EC therefore grants subsidies in excess of its quantity reduction commitment for sugar inconsistently with Articles 3.3 and 8 of the *Agreement on Agriculture*; and

• the EC's export subsidies for quota sugar, C sugar and ACP/India equivalent sugar are granted inconsistently with Articles 3.1(a) and 3.2 of the *SCM Agreement*;

• alternatively, if the Panel finds that the footnote is a valid qualification of the EC's substantive obligations under the *Agreement on Agriculture*, the EC is not complying with the terms of its footnote and is thus violating Articles 3.3, 8 and 9.1 of the *Agreement on Agriculture*.

• alternatively, if the Panel finds that the EC's subsidies on sugar are not export subsidies within the meaning of Article 9.1 of the *Agreement on Agriculture*, these subsidies are export subsidies that are applied in a manner which results in, or threatens to lead to, circumvention of the EC's export subsidy reduction commitments and are therefore inconsistent with Article 10.1 of the *Agreement on Agriculture*.

4.5 Brazil also requests that the Panel recommend to the DSB, in accordance with Article 19.1 of the *DSU* and Article 4.7 of the *SCM Agreement*, that the European Communities bring its export subsidies for sugar into conformity with its obligations under the *Agreement on Agriculture* by withdrawing without delay the export subsidies for sugar inconsistent with the *Agreement on Agriculture*.

4.6 In view of the remedy to which Brazil is entitled under Article 4.7 of the *SCM Agreement*, Brazil requests that the Panel make a finding and recommendation with regard to its claim under Article 3 of that Agreement. Brazil further requests that the Panel specify in its recommendation the time period within which the European Communities must withdraw the illegal portion of the export subsidies for sugar, and that the period not exceed the 90 days previous panels have allowed for withdrawal of prohibited subsidies.32

4.7 **Thailand** requests, for the reasons set out in its submission, that the Panel make the following rulings:

• the EC accords subsidies within the meaning of Article 9.1(c) of the *Agreement on Agriculture* to its exports of C sugar;

• exports of ACP/India equivalent sugar are covered by the EC's reduction commitments and are accorded subsidies within the meaning of Article 9.1(a) of the *Agreement on Agriculture*;

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• the quantity of sugar in respect of which the EC grants export subsidies within the meaning of Article 9:1 of the Agreement on Agriculture is in excess of its export quantity reduction commitment;

• the expenditures that the EC allocates for subsidies within the meaning of Article 9:1 of the Agreement on Agriculture to its exports of sugar are in excess of its budgetary outlay reduction commitment; and

• to rule in the light of these findings that the subsidies granted by the EC to its exports of sugar are inconsistent with Articles 3.3 and 8 of the Agreement on Agriculture;

• alternatively, if the Panel finds that the EC's subsidies on exports of sugar are not export subsidies within the meaning of Article 9:1 of the Agreement on Agriculture, these subsidies are export subsidies inconsistent with Article 10.1 of that Agreement;

• the EC's export subsidies for quota sugar and ACP/India equivalent sugar are granted inconsistently with Articles 3.1(a) and 3.2 of the SCM Agreement.

4.8 Thailand requests the Panel to recommend, in accordance with Article 19.1 of the DSU and Article 4.7 of the SCM Agreement, that the DSB request the European Communities to bring its export subsidies for sugar into conformity with its obligations under the Agreement on Agriculture by withdrawing within 90 days the export subsidies for sugar that are inconsistent with that Agreement.

4.9 For the reasons set out in its submissions, the European Communities requests the Panel to find that:

• exports of C sugar did not benefit from export subsidies within the meaning of Article 9.1(c) of the Agreement on Agriculture;

• the Complainants' claim under Article 10.1 of the Agreement on Agriculture was outside the terms of reference of the Panel; or,

• alternatively, exports of C sugar did not benefit from any "other export subsidies" within the meaning of Article 10.1;

• subsidiarily, exports of C sugar were not in excess of the EC's reduction commitments;

• subsidiarily, by bringing this claim, the Complainants were acting inconsistently with the general principle of good faith and Article 3.10 of the DSU;

• subsidiarily, the alleged inconsistencies did not nullify or impair any benefits accruing to the Complainants;

• the SCM Agreement did not apply to subsidies granted with respect to agricultural products or, to the extent that it did, that exports of C sugar did not benefit from export subsidies within the meaning of Article 3.1(a) of the SCM Agreement.

• footnote 1 was consistent with the Agreement on Agriculture;

• subsidiarily, by bringing this claim, the Complainants were acting inconsistently with the general principle of good faith and Article 3.10 of the DSU;
subsidiarily, the alleged inconsistency did not nullify or impair any benefits accruing to the Complainants;

to the extent that it was within the Panel's terms of reference, the claim that footnote 1 did not permit the EC's practice of exporting with refunds a quantity equivalent to the ACP/India imports was unfounded.

B. TERMS OF REFERENCE

1. Provisions and measures at issue

4.10 The European Communities submitted that certain issues brought by the Complainants constituted separate "claims" and thus fell outside the Panel's terms of reference.

4.11 The European Communities contended that, while the Complainants' panel requests cited Article 10.1 of the Agreement on Agriculture (but not Item (d) of the Illustrative List of Export Subsidies), none of the Complainants specified the measure which was allegedly inconsistent with that provision. In the European Communities' view, Article 10.3 of the Agreement on Agriculture did not relieve the Complainants of their obligations under Article 6.2 of the DSU. The Complainants had to identify, in their panel requests, "the specific measures at issue and provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly". The European Communities considered that the Complainants' claims under Article 10.1 of the Agreement on Agriculture failed to meet that standard. In particular, the allegation that the provision of C beet was an export subsidy within the meaning of Item (d) of the Illustrative List, was not an argument, but a "claim" on its own, which was not within the terms of reference of the Panel. Moreover, the European Communities continued, exports of sugar were not a "measure" within the meaning of Article 6.2 of the DSU. They were private transactions which could not, as such, be the subject of dispute settlement.

4.12 The European Communities submitted that a mere reference to the EC's "sugar regime" or to Council Regulation (EC) No. 1260/2001 (which consisted of 51 articles, with numerous paragraphs and subparagraphs, as well as 6 annexes, and covered 45 pages of the Official Journal of the European Communities) was not sufficiently "specific". Rather, the Complainants should have identified the specific elements of the EC's sugar regime which, according to them, provided the alleged export subsidies applied by the European Communities so as to circumvent its reduction commitments inconsistently with Article 10.1 of the Agreement on Agriculture. In the European Communities' opinion, the Complainants had failed to do so. For example, while the panel requests claimed that exports of C sugar were subsidized because they were made at prices below the average total cost of production of sugar, they contained no trace of what the European Communities considered as separate "claims" that: (a) the "exemption" of C beet from the minimum prices for A and B beet provided an export subsidy to the sugar producers; and that (b) there was a "payment" from European Communities consumers to EC sugar producers in the form of "artificially high" domestic prices for A and B sugar, as advanced by Brazil.

4.13 The European Communities submitted further that Brazil and Thailand had made a claim, on a subsidiary basis, regarding an alleged failure to respect the terms of the footnote in the EC's Schedule, which according to the European Communities, was not made in their panel requests. Consequently, the European Communities contended that these claims fell outside the terms of reference of the Panel.

4.14 The Complainants asserted that they had properly stated their claims in their panel requests, and specifically referred to the original texts in these requests. They denied having submitted, in their first written and oral submissions, further legal claims involving separate legal provisions or measures
different from those presented in their respective panel requests. In their view, the European Communities was confusing "claims", which must be stated in panel requests, with "arguments", to be developed in the course of the Panel's proceedings. According to the Appellate Body, Article 6.2 of the DSU required that the claims, but not the arguments, had to be sufficiently specified in the request for the establishment of a panel in order to allow the defending party and any third parties to know the legal basis of the complaint.\(^\text{33}\)

4.15 The Complainants stressed that the European Communities' contentions had to be examined in light of Article 10.3 of the Agreement on Agriculture. Because of the reversal of the burden of proof, it was not incumbent on them to identify or enumerate the WTO agreements, provisions, or export subsidy definitions that the European Communities might choose to invoke in its defence. It was the European Communities' duty to prove that no subsidy of any kind, under any WTO agreement, had been granted by any EC measure to sugar exports in excess of its reduction commitments. In the Complainants' view, any and all EC measures that might confer a subsidy on these sugar exports, any and all WTO agreements with subsidy provisions were thus within the terms of reference of the Panel by virtue of Article 10.3 of the Agreement on Agriculture. In particular, since the scope of Article 10.1 of the Agreement on Agriculture extended to export subsidies as defined in the WTO agreements other than those listed in Article 9.1, the Article 10.1 obligation was not contingent on a claim of inconsistency with the provisions of the SCM Agreement or any other WTO Agreement. For the Complainants, the export subsidy definitions of GATT 1994 had application to the export subsidies covered by the provisions of Article 10.1 of the Agreement on Agriculture.

4.16 The Complainants also countered that they had sufficiently identified the regulations that were likely to be relevant in the present dispute in their requests for consultations, in their respective requests for the establishment of a panel, as well as in their first submissions. They considered the reference to (EC) Council Regulation No. 1260/2001 to be sufficiently specific to meet due process requirements. For example, Article 10.1 of the Agreement on Agriculture had been clearly identified in their respective panel requests as a claim in the alternative in relation to their basic claim regarding exports in excess of export subsidy reduction commitments. To allege subsidized exports in excess of reduction commitments as well as an inconsistency with Articles 3.3 and 8 of the Agreement on Agriculture was sufficient, in their view, to meet the requirements of Article 6.2 of the DSU. By virtue of Article 10.3, it was then up to the exporting Member to prove that "no export subsidy, whether listed in Article 9 or not, has been granted with respect to" those exports of sugar in excess of reduction commitment levels. Imposing the requirement on the Complainants to identify all "other" export subsidies individually would have the effect of limiting the burden of the exporting Member, re-reversing the burden of proof of Article 10.3 as applied to Article 10.1, and ultimately rendering Article 10.3 meaningless and ineffective, contrary to the basic rules of treaty interpretation.

4.17 Australia added that the European Communities would fall short of meeting its own standard given that, on a number of occasions it had used comparable language in its own panel requests. Brazil underlined that while it was theoretically possible that some subsections of EC Regulation No. 1260/2001 played no role in the provision of the challenged subsidies, Brazil's failure to identify and expressly exclude any of those subsections from its description of the measure at issue would not mean that Brazil had not properly identified the measure at issue within the meaning of Article 6.2 of the DSU. Australia and Brazil refuted the European Communities' contention that their panel requests only covered certain "payments", as suggested by the European Communities. In their opinion, the existence of payments was only one aspect of the subsidies at issue in the present dispute. Australia emphasized that the measures at issue were clearly identified in its panel request as the subsidies provided by the European Communities in excess of reduction commitment levels. Australia identified the source of the subsidization and the nature of legal complaint, including the

\(^{33}\) Appellate Body Report on EC – Bananas III, para. 143.
relevant legal provisions. Australia noted that the precise nature of the "payments" under Article 9.1(c) were legal arguments that did not have to be included in the panel request.

4.18 Furthermore, in the Complainants' view, nothing prevented them from anticipating the European Communities' rebuttal arguments, either in their first written submissions or in their rebuttal submissions. Article 9.2(b)(iv), for example, was brought into the case by the Complainants as a counter-argument, not as a claim of inconsistency, in response to arguments made by the European Communities. As the European Communities itself had raised the footnote as justification for non-compliance with its obligations, the Complainants were entitled to provide rebuttal arguments in that context, citing any WTO provisions, any EC laws or regulations, or other factual evidence. The Complainants had referred specifically to Article 9.2(b)(iv) to underline that the footnote, even if interpreted as imposing a quantity limit, would lead the European Communities to act inconsistently with its obligations by failing to achieve the reductions required by that provision. As a consequence, the European Communities would be providing export subsidies in contravention of the Agreement on Agriculture – a violation of Article 8, which undisputedly was within the terms of reference. The Complainants reiterated that such rebuttal arguments needed not be mentioned in the panel requests, and that, in the present case, their assertions regarding the scope of application of the footnote were thus subsidiary arguments supporting their basic legal claim that the European Communities was exceeding its export subsidy reduction commitments.

4.19 The European Communities maintained its argumentation. Thus, of the several claims raised by the Complainants with respect to C sugar under Article 9.1(c) of the Agreement on Agriculture, only one was properly before the Panel, i.e. the claim that exports of C sugar were "payments on exports" because they were made below average total cost of production. With respect to the footnote in the EC's Schedule, the European Communities contended that any suggestion that the European Communities was acting inconsistently with Article 9.2(b)(iv) of the Agreement on Agriculture had appeared for the first time during the first substantive meeting of the Panel, not in the requests for panel establishment, nor in the first written submissions of the Complainants, but only in the first oral statements of Brazil and Thailand. Since that provision was not mentioned in the Panel's terms of reference, it could not form the basis for a finding of inconsistency with any other provision of the Agreement on Agriculture. Nor had any of the Complainants set out a brief summary suggesting that the alleged failure of the European Communities to respect the terms of the footnote was the legal basis of their complaint. In the European Communities' view, the Complainants should have claimed that the European Communities did not, in fact, re-export ACP/India sugar but rather exported an equivalent amount. This would have required a reference to, and identification of, the footnote, because that was the legal provision allegedly infringed. The European Communities also considered that this was necessarily a separate claim, because it was premised on the assumption that the footnote was a valid justification for the European Communities exceeding its commitments, but that the footnote did not sanction an excess in respect of ACP/India equivalent sugar but only re-exported ACP/India equivalent sugar. As proof that the alleged non-respect of the footnote was a separate claim, the European Communities observed that Brazil and Thailand had made the "claim" as an "alternative claim." However, the corresponding legal basis was not set out in the requests for establishment of a panel.

4.20 The European Communities acknowledged that Article 10.3 of the Agreement on Agriculture relieved the Complainants from the obligation of having to prove their claim that the European Communities granted export subsidies in excess of its reduction commitments. In its view, however, Article 10.3 did not exempt the Complainants from identifying, in their panel requests, the relevant measures that provided the alleged export subsidies, in accordance with Article 6.2 of the DSU (see also paragraph 4.12). Moreover, the European Communities observed that Article 10.3 was not listed among the special or additional rules and procedures on dispute settlement in Appendix 2 to the DSU and thus did not derogate from the requirements imposed by Article 6.2 of the DSU. The European Communities further considered that the issue of who should bear the burden of proof should not be
confused with the distinct issue of who must state the claims. The Complainants' interpretation of Article 10.3 would be incompatible with the basic requirements of due process because it would impose upon the European Communities the impossible task of identifying all the conceivable export subsidies. The inversion of the burden of proof could not have the consequence of depriving the defending party of the fundamental procedural right "to know what case it has to answer and what violations have been alleged".  

4.21 The Complainants reiterated that they had shown that EC exports of sugar exceeded its reduction commitments (see paragraphs 4.28-4.29). Unless the European Communities could prove that the excess was not subsidized, the European Communities was acting inconsistently with its obligations under Articles 3.3 and 8 of the Agreement on Agriculture, and Article 3 of the SCM Agreement. If the European Communities could not prove that the excess was not subsidized, no other provisions of the agreements were relevant. But if the European Communities claimed that the excess was not subsidized, or that reduction commitments did not apply to all or part of the excess, then the Complainants were entitled to raise, by way of counter-arguments, any WTO provisions, as well as any EC laws or regulations, or other factual evidence, to rebut the EC claims. In the Complainants’ views, none of these rebuttal arguments or evidence needed to be mentioned in their requests for panel establishment.

2. Procedural matters

4.22 Australia observed that the European Communities did not raise any concerns in regard to alleged deficiencies in its panel request until six months after the Panel was established and more than two months after the Panel was composed. The European Communities did not raise any concerns with respect to the establishment of the Panel nor did it seek a preliminary ruling at an early stage of the Panel process, actions it had taken in recent disputes in which it was a respondent. Instead, the European Communities had waited until its first written submission to raise concerns in regard to Article 10.1. Nor had it sought to discuss the issue with Australia, in the context of the opportunity provided by Article 7 of the DSU to modify the standard terms of reference. In this regard, Australia recalled that the principle of good faith under Article 3.10 of the DSU required respondents to act promptly in identifying procedural deficiencies and bringing them to the attention of the complaining Members, and to the DSB, or the Panel.

4.23 Brazil was of the opinion that the European Communities had not made any credible attempt to show that it had suffered prejudice in the conduct of its defence due to an alleged lack of clarity or deficiencies in the panel request. According to Brazil, a showing of prejudice was essential to any argument that a claim had not been set out with sufficient specificity in a panel request.

4.24 In response, the European Communities first recalled that its objection related to the fact that it could not identify, in the panel requests, some of the "claims" stated by the Complainants in their first submissions. The European Communities, therefore, could not have complained before receiving the Complainants' first submissions. Secondly, although it had suffered a prejudice, the European Communities did not agree that it was required to show prejudice, because that requirement was not mentioned in Article 6.2 of the DSU.

C. Burden of Proof

4.25 The Complainants submitted that, under Article 10.3 of the Agreement on Agriculture, the burden of proof rested with the European Communities to demonstrate that no export subsidy, whether listed in Article 9 of the Agreement on Agriculture or not, had been granted to sugar exports in excess of the European Communities' reduction commitment level.

4.26 Drawing attention to the analyses by the Appellate Body in a number of cases\textsuperscript{35}, the Complainants held that they only bore the burden of proof in relation to the \textit{quantitative aspect}, i.e. that the European Communities was exporting quantities in excess of its scheduled reduction commitment level. If the Complainants met this burden and the European Communities contested the \textit{export subsidization aspect} of the claim, then the European Communities had an obligation, or legal burden, to establish that no export subsidy had been granted to the quantity exported in excess of the reduction commitment level specified in its Schedule. According to the Complainants, this analysis applied to their claims under Articles 3, 8, 9 and 10.1 of the \textit{Agreement on Agriculture}.\textsuperscript{36}

4.27 The \textbf{European Communities} agreed that it would have the burden of proof under Article 10.3 of the \textit{Agreement on Agriculture} with respect to the "subsidization aspect" of the Complainants' claim, assuming that the Complainants had met their burden of proof with respect to the "quantitative aspect" of their claims. However, the European Communities held that some of the Complainants' "claims", in its view, had not been properly stated in the panel requests as required by Article 6.2 of the \textit{DSU}, and were therefore outside the terms of reference of the Panel (see paragraphs 4.10-4.13 and 4.19-4.20).

1. \textbf{Quantitative aspect}

4.28 In order to discharge their burden of proof in respect of the quantitative aspect of their claims under Articles 3, 8, 9 and 10.1 of the \textit{Agreement on Agriculture}, the Complainants referred to the European Communities' notifications to the Committee on Agriculture.\textsuperscript{37} The notified data showed that the European Communities had exported 4.097 million tonnes of sugar in the 2001-2002 marketing year. The Complainants pointed out that this figure, which excluded food aid, represented more than three times the scheduled quantity reduction commitment level of 1.273 million tonnes, and underlined that in every marketing year since 1995, the European Communities had exported sugar in amounts three to four times the level of its reduction commitments. The Complainants stressed that it was the fact that the European Communities' total exports of sugar exceeded the European Communities' reduction commitment levels that mattered, regardless of how the sugar was categorized. Having met their burden of proof in respect of the quantitative aspect of their claim, the Complainants noted that the European Communities did not contest the supplied factual evidence.

4.29 The Complainants indicated that, to the best of their knowledge, most, if not all, of the excess exports, were accounted for by the C sugar and ACP/India equivalent sugar categories. With particular reference to ACP/India "equivalent" sugar, \textit{Australia} and \textit{Thailand} observed that, during the marketing year 2001-2002, the European Communities notified export subsidies amounting to €482.8 million against a scheduled budgetary outlay reduction commitment of €499.1 million but excluded from its reduction commitments some €800 million in direct export subsidies on 1.6 million tonnes of sugar from its reduction commitments. Similarly, quantity commitments had been exceeded by 1.378 million tonnes.

4.30 The \textbf{European Communities} admitted that current exports of sugar were in excess of the figure shown in the EC's Schedule. However, this did not mean that the European Communities had breached its export subsidy reduction commitments; rather the Complainants' claim was based on a misunderstanding of the information contained in the EC's Schedule.


\textsuperscript{37} Exhibit COMP-17.
4.31 The European Communities explained that it did not grant any export subsidies to exports of C sugar. However, if the Panel were to find that C sugar indeed benefited from export subsidies, the European Communities submitted that its sugar exports would not be in excess of the reduction commitments when those were interpreted in good faith and in the context of the Modalities Paper. With respect to ACP/India equivalent sugar, the European Communities submitted that the burden of proving their case rested with the Complainants because they had also misinterpreted the footnote. In the European Communities’ view therefore, exports of ACP/India equivalent sugar were not in excess of its scheduled commitments, when these were interpreted in good faith.  

2. Export subsidization aspect

4.32 The Complainants submitted that, as the party claiming that the excess quantity was not subsidized, the European Communities had the obligation to demonstrate that such excess had not been granted export subsidies. In other words, that none of the Article 9.1 listed subsidies had been granted in respect of the quantity of sugar that was exported in excess of the European Communities’ scheduled reduction commitment level; and no "other" export subsidies were being applied to such sugar exports, for the purposes of Article 10.1. The Complainants held that, if the European Communities did not produce any evidence in that regard, it would have failed to establish that an export subsidy was not being applied to sugar, within the meaning of either Article 9.1 or Article 10.1 of the Agreement on Agriculture.

4.33 The European Communities responded that the Complainants' interpretation of Article 10.3 of the Agreement on Agriculture was incompatible with the basic requirements of due process because it would impose upon it the impossible task of identifying all the conceivable export subsidies which, the European Communities held, it did not grant. The inversion of the burden of proof could not possibly have the consequence of depriving the defending party of this fundamental procedural right. Referring to the Appellate Body's analysis in Canada – Dairy, the European Communities indicated that it was not requesting that the Complainants make a prima facie case that the elements of the "claimed exports subsidies" were present. Rather, the European Communities contended that the export subsidization aspect was also part of the claim to be made by a complaining party, and that Article 10.3 did not exempt the Complainants from identifying the relevant "payments" that provided the alleged export subsidies.

4.34 The Complainants reiterated that the European Communities had failed to discharge its burden of proof in its submissions and in panel hearings. As already indicated in paragraph 4.18 above, Article 10.3 of the Agreement on Agriculture did not require them to lead in the presentation of evidence to the Panel in relation to the export subsidization aspect. Nevertheless, for reasons of procedural efficiency, but without relieving the European Communities of its burden, and without waiving their rights under Article 10.3 of the Agreement on Agriculture, the Complainants had addressed several points in their respective submissions, but only in anticipation of arguments that they expected the European Communities to submit.

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38 The parties' arguments in respect to these claims are presented in Section IV.D with respect to C sugar, and in Section IV.E with respect to ACP/India equivalent sugar.
41 See Section IV.B, Terms of reference.
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4.35 With respect to C sugar, the Complainants recalled that, by subsidizing exports in excess of its reduction commitments\(^{42}\), the European Communities had acted inconsistently with Articles 3.3, 8, and 9.1(c) or, alternatively, 10.1 of the Agreement on Agriculture, and that the European Communities had the burden of proof (see Section IV.C above).

1. Article 9.1(c) of the Agreement on Agriculture

4.36 The Complainants submitted that C sugar benefited from export subsidies falling within the description of Article 9.1(c) of the Agreement on Agriculture and observed that Article 9.1(c) subsidies were subject to reduction commitments in accordance with the provisions of Article 9.1. A measure that met the description of any of the subparagraphs (a) through (f) of Article 9.1 was, by definition, an export subsidy and, as such, necessarily subject to the reduction commitments of the scheduled product in question. They pointed out that Article 9.1 was, in that respect, similar to the Illustrative List of Export Subsidies in Annex I of the SCM Agreement. Since the European Communities had not subjected C sugar to the required quantity reduction commitments, the Complainants argued that the non-inclusion of C sugar in the quantity reduction commitments was inconsistent with Article 9.1, and thus with Articles 3.3 and 8, of the Agreement on Agriculture.

4.37 The European Communities replied that the exports of C sugar did not benefit from export subsidies falling within Article 9.1(c) of the Agreement on Agriculture or from any "other export subsidy" within the meaning of Article 10.1. Moreover, even if exports of C sugar were found to benefit from export subsidies, the European Communities submitted, subsidiarily, that those would not exceed the reduction commitments scheduled by the European Communities, or, if they did, would do so by much less than claimed by the Complainants, if the reduction commitments were interpreted in good faith and taking into account the context provided by the Modalities Paper (see also Section IV.D.3(a)).

(a) "Payment"

4.38 The Complainants first recalled the Canada – Dairy jurisprudence, on which they had principally based their arguments. They asserted that, in order to determine whether a payment had been made, an examination was needed of all monetary and non-monetary economic costs of production, i.e. whether the price of the exported agricultural product at issue reflected all the economic resources invested in the production of that product\(^{43}\), not only those invested by the economic operator who engaged in the processing or export of C sugar. They recalled that a "payment" within the meaning of Article 9.1(c) denoted a "transfer of economic resources" whether in the form of money or in some other form which conferred value such as payments-in-kind; that it "may take place in many different factual and regulatory settings"\(^{44}\) and that it was not limited to payments by governments, but could be made and funded by private parties.\(^{45}\) The existence of a payment-in-kind would be determined by comparing prices with an objective standard, reflecting the proper value of the product to the producer.\(^{46}\) The appropriate benchmark for ascertaining if a payment was made was whether the prices paid to the producers were below the "total cost of production".\(^{47}\) This benchmark represented an objective standard against which to assess whether the

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\(^{42}\) Exhibit COMP-17.
\(^{47}\) Ibid., paras. 71, 76, 86-87 and 114.
prices paid were sufficient for producers to recover the average fixed and variable costs of production and thus avoid making "losses" over the longer term. 48 Furthermore, since the international obligations of the European Communities, not of its member States, were at issue in the present case, the benchmark had therefore to be a single, Community-wide, cost of production figure rather than the cost of production figures for each individual EC member State. 49

4.39 **Australia** identified a "payment" on C sugar in that it was being sold at below the average total cost of production by the sugar producer to the world market. Australia defined "producer" as a collective term for all enterprises engaged in the production of sugar, from the growing of sugar beet or cane to the processing/refining of sugar from sugar beet or sugar cane or from raw cane sugar. The transfer of resources in this case was from the EC sugar producer to the purchaser, in that the price charged by the producer of the sugar was less than the proper value of the sugar to the producer. According to Australia, the export production received an advantage because the payment was financed by virtue of governmental action. In response to additional questions from the Panel, Australia went on to identify other "payments" within the production chain which involved sales at prices that did not reflect the "proper value" of the product to the producer. In respect of these payments, Australia indicated however that while, in its view, they clearly fell within the definition of Article 9.1(c), and were indistinguishable from the Canada – Dairy case, it was not necessary to dissect the structure of the EC sugar regime to find a payment. These payments were as follows: 50

(a) the "payment" from the beet grower to the sugar processor in the form of beet sold below its proper value to the grower, i.e. beet sold below its costs of production. As set out in the evidence presented by Australia, C beet was categorized into C1 and C2 beet in the main C sugar-producing countries, with C2 beet being priced on the basis of an approximately *** split of revenue from C sugar sales. Over the 11 years to 2002-03 the payment for C2 beet was estimated to have averaged *** per cent of the average total cost of producing beet in France and *** per cent in Germany. Therefore, for sugar produced from C2 beet, Australia submitted that there was a payment-in-kind, in the form of beet sold below its proper value, by the growers to the processors. 51

(b) a sale by the sugar processor to the exporter: in most cases that Australia was aware of, that sugar was sold onto the world market via an exporter. The exporter purchased the sugar from the sugar processor and then sold it onto the world market. The price paid by the exporter was, in the case of all C sugar exports, below the total average costs of production. Thus, Australia submitted that there was a payment-in-kind from the sugar processor to the sugar exporter in the form of sugar below its production costs which enabled the exporter to sell the sugar onto the world market.

4.40 **Brazil** noted that there may be multiple "payments" within the meaning of Article 9.1(c) involved in the production and sale for export of a single product such as sugar. 52 Brazil underlined that it could have simply shown that C sugar was being sold for export below the average total cost of production, but that it went further and identified three examples of "payments" within the meaning of Article 9.1(c) that occurred in the process of production and export sale of C sugar, and which gave "an advantage" to "export production" of C sugar. These "payments" were as follows:

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50 Australia’s first written submission, paras. 111-113; see also Australia’s replies to Panel questions 46-48.
51 Exhibit ALA-1, pp 10-11; Australia’s reply to Panel question 62.
52 Brazil’s first written submission paras. 42-49; Brazil’s replies to Panel questions 46-48 and 62.
(a) High internal prices paid by EC consumers, through a combination of governmental actions such as intervention prices, quotas, export refunds and import restraints, to processors of C sugar. 53  According to Brazil, a similar payment was made by EC taxpayers who were taxed to support export refunds. The transfer of economic resources consisted of the transfer of money from the consumers and taxpayers (the "payers") to the processors and exporters (the "payees"). Through these "payments", the export of C sugar at prices below the average total cost of production of C sugar was facilitated;

(b) A "payment" was found in the EC sugar regime's requirement for minimum prices for A and B quota beet, which enabled beet growers to sell C beet to processors at prices below its cost of production. Such a "payment" constituted a transfer of economic resources in the form of a payment-in-kind to the sugar processors. Brazil underlined that, in this case, the "payers" were the beet growers who transferred C beet to the processors (the "payees") at prices that did not reflect the cost of production of the beet. Brazil noted that although prices between growers and processors for C beet were not regulated by the EC, available evidence indicated that the growers normally received *** per cent of the world market price for a large portion of C beet, except for that portion that was treated as C1 beet. 54  This price was far less in monetary terms than the 58 per cent of the intervention price that growers received for A and B beet, and far below the average total cost of producing beet. 55

(c) A third "payment" was found in the export sale of C sugar on the world market at prices below its average total cost of production. This "payment" constituted a payment-in-kind by the producers (the "payers"), who transferred resources provided by the European Communities to the world market buyers of this sugar (the "payees"). The world market buyers gained access to this sugar supply at prices below its average total cost of production. Brazil submitted that, by enabling C sugar producers to make this payment-in-kind, the EC regime conferred an advantage to EC export production, notwithstanding the fact that the exporters themselves "made" the payment.

4.41 Calling for a sector-wide approach, Thailand submitted that, in light of the Canada – Dairy jurisprudence summarized in paragraph 4.38 above, there was no requirement to distinguish between C sugar sold to exporters, C sugar sold abroad, and C beet sold to processors, or to identify the individual transactions through which the payments were made, or to examine, in a disaggregated manner, the "payments" made by beet farmers and those made by sugar processors. All that was required in order to determine the existence of a "payment" was a comparison between the average total cost of production of all operators involved in the production of C sugar and the average price at which C sugar was sold for export. Thailand nonetheless stated that it would have no objection if the Panel were to examine separately the payments, including those made by beet farmers and those made by sugar processors. 56

4.42 The Complainants contended that the existence of "payments" within the meaning of Article 9.1(c) of the Agreement on Agriculture could be established from data on costs of production.

53 Exhibit COMP-1, para. 81. In particular, the Court of Auditors reported that the annual cost to the budget of surplus sugar was approximately €1,500 million, some €800 million of which were obtained from production levies on A and B quota sugar, with the balance paid for by European taxpayers. 54 Exhibit COMP-1, C 50/11, para. 16.  55 Exhibit BRA-1, Table 5.  56 Thailand's replies to Panel question 62.
and returns on world markets. They submitted production cost data\textsuperscript{57} which showed that, for the marketing years 1992/93 to 2002/03, beet growers failed to recoup between *** and *** per cent of their total cost of producing C beet. These losses were financed by the very high returns received by the growers of beet for A and B quota sugar. During the same period, the processors failed to recover between *** and *** per cent of their total cost of production of C sugar, while export market returns from C sugar represented *** per cent of the average total production costs.\textsuperscript{58} Further statistical evidence\textsuperscript{59} showed that, while the average total cost of sugar production in the European Communities was higher than the prices received for C sugar on the world market, C sugar continued to be exported in what the Complainants considered to be significant quantities. In their view, the losses would be unsustainable in normal commercial operations if processors were to produce only C sugar. The fact that there was no independent production of C sugar confirmed that C sugar could not be produced absent a payment.

4.43 Citing various studies\textsuperscript{60}, the Complainants contended that in 2002/03, the Community-wide cost of production of all sugar in the European Communities was *** per tonne. At the same time, the world market price for sugar (as measured by the London Daily Price) was on average €144.88 per tonne, which was less than *** per cent of the cost of production in the European Communities, implying that the cost of producing sugar was more than *** times the price that same sugar commanded on the world market. The Complainants pointed to the assessments undertaken by the European Communities' own official bodies, which had acknowledged that the gap between the cost and the price of C beet and C sugar was financed by virtue of the governmental action taken by the European Communities through its sugar regime.\textsuperscript{61} According to the Complainants, the figures also showed that for the entire period from marketing year 1992/93 through 2002/03, although C sugar prices were below average total costs, these prices exceeded marginal costs. Thus, C sugar prices were able to generate a positive contribution to net income once marginal costs were covered.\textsuperscript{62} Whichever method was considered the most accurate for estimating the world market price, the price received for C sugar was invariably lower than the average cost of producing C sugar (see also paragraph 4.74 et seq.).

4.44 The European Communities responded that only one of the payments cited by the Complainants was properly before the Panel, i.e. the payments-in-kind from EC sugar producers in the form of export sales of C sugar below total average cost of production. The EC considered that each of the other "payments" alleged by the Complainants constituted a distinct claim that was not within the Panel's terms of reference (see Section B above, Terms of reference). While raising doubts regarding the precise nature of those "payments" and the way in which they would provide an export subsidy within the meaning of Article 9.1 (c.) of the Agreement on Agriculture, the European Communities disagreed that the prices paid by the EC consumers for A and B sugar involved "payments". The EC consumers paid the prevailing domestic market price and, therefore, transferred no "economic value" to the sugar producers.

4.45 In the European Communities' view, the Complainants had misread the jurisprudence in Canada – Dairy, on which they were basing their claims and allegations. The Canada – Dairy cases concerned different factual circumstances involving the provision of an agricultural input below its

\textsuperscript{57} Exhibit ALA-1, pp 9; Exhibit COMP-2, Table 2.1, pp. 8-9; Exhibit BRA-1, Table 5, p. 29; Diagram 2, para. 18.

\textsuperscript{58} Exhibit ALA-1, p. 9.

\textsuperscript{59} Including official EC and member State documentation, OECD papers, studies of research institutes, information available from the private sugar sector as well as confidential LMC data.

\textsuperscript{60} Exhibit BRA-1, Annex B, Table B.15, and Table 5, p. 29; Exhibit COMP-2, para. 3.9, p. 43.

\textsuperscript{61} Exhibit COMP-1, C 50/16, para. 96.

\textsuperscript{62} Exhibit BRA-1, para. 18; Diagram 2.

\textsuperscript{63} Ibid., para. 43(a); Diagram 11.
average total cost of production which constituted a "payment" to the processor of that input. If that payment was "financed by virtue of government action", and if it was contingent on the subsequent exportation of the processed product, only then was the processed product deemed to benefit from an "export subsidy" subject to reduction commitments.

4.46 The European Communities considered that the Complainants' allegations in paragraphs 4.38-4.42 would imply that the producers of C sugar were at the same time the providers and the recipients of the alleged export subsidy, and that C sugar was at the same time the subsidized product and the product which conferred the export subsidy. The European Communities contended that, insofar as the sales of C sugar involved a "payment", the recipient of such payment and, therefore, of the alleged subsidy, would be the foreign buyers of C sugar, rather than the producers of C sugar. In turn, the goods subsidized by such payments would not be the exports of C sugar, but instead the goods manufactured by the foreign buyers of C sugar into which C sugar was incorporated.

4.47 While a cost of production benchmark may be appropriate in certain cases where sales were made within the domestic market, the European Communities continued, it would not always be so, as illustrated by the first Canada – Dairy case. The Appellate Body had emphasized that in order to establish the existence of a "payment", it was "necessary to scrutinize carefully the facts and circumstances" of the measure at issue in each case. Furthermore, even if the provision of C beet constituted a "payment on exports", the Complainants would still have to show that it was "financed by virtue of governmental action". In this regard, the European Communities considered that the Complainants had overlooked some important differences between the production of milk at issue in Canada – Dairy, and the production of C beet. The availability and the cost of C beet could vary greatly between EC regions, as well as from one year to another, depending on a multiplicity of factors, which did not involve "governmental action", or at least the type of action at issue in this dispute. For example, the production of beet was affected by climatic conditions and diseases to a much greater extent than the production of milk. Also, beet farmers were much less specialized than milk farmers as beet was produced on a rotational basis. As a result, the production of C beet, according to the European Communities, was as likely to be "financed" by A and B beet as by other alternative crops, and vice versa. For those reasons, the "causal link" between the alleged "governmental action" and the provision of C beet was not "tight" enough to consider that sales of C beet were "financed by virtue of governmental action".

4.48 The European Communities further submitted that the cost of production of sugar was not a relevant benchmark in order to establish whether export sales of C sugar involved "payments". Instead, the relevant benchmark was the world market price for sugar. The European Communities held that the Appellate Body had resorted to a cost of production benchmark in view of the specific circumstances of Canada – Dairy. That benchmark could not be mechanically applied to the present case but it might be appropriate in situations where, as in Canada – Dairy, the sales were made within the domestic market. However, when the sales were made in the world market, the only relevant benchmark for determining the existence of "payments" was the price prevailing in that market.

The use of a cost of production benchmark in cases involving input subsidies to exported goods was supported by Items (j) and (k) of the Illustrative List of the SCM Agreement, as explained by the Appellate Body. Those two provisions were not concerned with the export of goods below cost of production, but instead with the granting of subsidies to exported goods through the provision of

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64 Exhibit EC-10, paras. 46-49; Exhibit EC-11, paras. 16-17. Since, according to the European Communities, the alleged payments would not, in any event, provide an export subsidy to C sugar according to the Appellate Body's interpretation, the European Communities did not consider it necessary to revisit these two issues, but reserved the right to raise them in the event of an appeal.


66 Ibid. para. 93.
certain financial services (export credits, guarantees and insurance) at a price below the cost to the
dispute, Items (j) and (k) of the Illustrative List were concerned with input subsidies.

4.49 Recalling that Article 9.1(c) did not identify any specific benchmark, and that the examination
of whether a measure involving "payments" had to be made, in each case, having regard to the
"factual and regulatory setting of the disputed measure"\textsuperscript{67}, the European Communities drew attention
to the reasoning of the Appellate Body with respect to the "administered domestic price"\textsuperscript{68}, as well as
with world market prices\textsuperscript{69}, when these had been considered for their relevance as possible
benchmarks in \textit{Canada – Dairy}:

"... a comparison between CEM prices and world prices gives no indication on the
crucial question, namely whether Canadian export production has been given an
advantage. Furthermore, if the basis for comparison were world market prices, it
would be possible for WTO Members to subsidize domestic inputs for export
processing, while taking care to maintain the price of these inputs to the processors at
a level which equalled or marginally exceeded world market prices."\textsuperscript{70}

4.50 According to the European Communities, this statement was additional proof that the
Appellate Body's decision not to use the world market price as a benchmark in \textit{Canada – Dairy} was
linked to the fact that the alleged "payments" consisted of the provision of inputs for processing
within Canada (see also paragraph 4.45). The European Communities asserted that the mere fact of
exporting goods below the average total cost of production provided no "advantage" to that "export
production", unlike the provision of inputs below cost within the exporting country.

4.51 The European Communities submitted further that the alleged payments conferred no
"benefit" to C sugar and that the Complainants' interpretation of Article 9.1(c) would make it possible
to establish the existence of an export subsidy in a situation where, far from receiving a benefit
through the alleged subsidy, the supposed recipient of the subsidy was in fact making a financial
contribution and providing a benefit to another operator in another Member. The European
Communities reasoned that if the sales of C sugar involved a "payment", it would follow that the
producers of C sugar were foregoing part of the sugar's "proper value" to them. Insofar as the C sugar
producers received a benefit, such benefit was not conferred by the "payments" themselves, but
instead by the previous "financing" of the payments "by virtue of governmental action". Such
government "financing", however, did not necessarily involve a subsidy and, even if it did, it was not
contingent upon export performance. According to the European Communities, the Complainants'
interpretation of Article 9.1(c) would render inapplicable the other constituent element of the notion
of subsidy, i.e. the requirement that the measure provided a "benefit". It would transform
Article 9.1(c) into a \textit{per se} rule against exports below cost of production, totally disconnected from
the existence of subsidization. Article 9.1(c) would then become a form of anti-dumping instrument,
which was not even found in the Anti-Dumping Agreement. The European Communities contended
that neither the \textit{Agreement on Agriculture} nor its drafting history contained any suggestion that the
drafters had intended to impose stricter disciplines against the dumping of agricultural products
through Article 9.1 (c).

4.52 Responding to the European Communities' argument in paragraphs 4.45, 4.48, and 4.50
above, the \textbf{Complainants} held that the legal reasoning and conclusions in \textit{Canada – Dairy} were not
limited to the specific case of subsidized inputs for processing, and that the citations mentioned were

\textsuperscript{67} Ibid. para. 76.
\textsuperscript{68} Ibid. para. 81.
\textsuperscript{69} Ibid, para. 83.
\textsuperscript{70} Ibid, para. 84.
not only intended to explain the factual situation existing in that case. To the contrary, the Complainants reaffirmed that, on the basis of the jurisprudence cited in paragraph 4.38, neither the text of Article 9.1(c), nor Canada – Dairy, limited the universe of export subsidies or payments as alleged by the European Communities. The Appellate Body had interpreted the precise provision that the Complainants had argued was being breached in the present case, i.e. Article 9.1(c). In their view, the European Communities’ assertion would imply that no Appellate Body or panel reports would be considered relevant because of differing factual situations.

4.53 The Complainants considered that, even if Canada – Dairy were to be construed in the limited manner suggested by the European Communities, the present case fitted directly within the scope of that case because one of the “payments” at issue involved the sale of C beet (a primary product) to sugar processors at below the average total cost of production. The Complainants went on to underline the similarities between the milk regime in Canada – Dairy and the sugar regime in the present case. Both were quota-based systems delivering price support; in both cases the product at issue was manufactured from a primary product, and the final product had to be exported; “governmental action” provided the supply of the primary product at prices below that for which the same product could be sold on the domestic market; and in both cases the primary product was sold at below the average total cost of production and the losses were financed by the governmental action.

4.54 The Complainants further argued that there was nothing in the wording of Article 9.1(c) and the rulings of the panel and Appellate Body in Canada-Dairy to suggest that Article 9.1(c) only applied to payments made in the form of sales of inputs to domestic processors. If the European Communities’ argument were correct, Article 9.1(c) would not, for example, apply to cases involving agricultural products that needed no processing prior to exportation; products that were processed by farmers themselves; those processed by cooperatives or other entities owned by the farmers; or those which farmers exported for processing abroad. Therefore the Complainants contended that if Article 9.1(c) were interpreted to exclude such products, a distinction would be made that was completely divorced from the purpose of that provision, and Members would be given the opportunity to escape their export subsidy reduction commitments simply by integrating the production and processing of agricultural products. An acceptance of the European Communities’ interpretation would therefore defeat the purpose of Article 9.1(c).

4.55 In the context of the application of Article 9.1(c), the Complainants continued, the factual situation in regard to C sugar was even more compelling given the emphasis by the Appellate Body on the importance of maintaining the distinction between the domestic support and export subsidies disciplines in the Agreement on Agriculture. That distinction had been ignored by the European Communities. In this way, the European Communities was eroding the rights of other WTO Members accruing from its export subsidy commitments and obligations under the Agreement on Agriculture, as the level of C sugar exports, as well as the European Communities’ overall sugar exports, had increased over the period 1995 to the present. Since, unlike in the Canadian milk regime, there were no independent producers of either C beet or C sugar in the European Communities, cross-subsidization was total. Moreover, all C sugar was exported at prices below cost of production with the losses financed from the sales of quota sugar in the domestic and export market with the benefit of EC price support. The level of C sugar production as a percentage of total production was much higher than in the Canadian dairy regime. The difference between the costs of production and the returns on C sugar was equally higher, implying a higher level of cross-subsidization.

4.56 The Complainants maintained that the cross-subsidies provided from price support were captured by WTO definitions of subsidies contingent on export performance. They considered that the European Communities’ arguments conflicted with the jurisprudence of Canada – Dairy as they rested on the proposition that domestic price support could never form part of an export subsidy

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definition within the meaning of Article 9.1(c). On the contrary, subsidization of exports through legitimate price support had been captured by export subsidy definitions since the early days of GATT. The fact that the system of income or price support constituted a subsidy contingent on export performance was irrelevant. The real issue, according to the Complainants, was whether such support, in whole or in part, came within the definitional scope of an export subsidy within the meaning of Article 9.1(c) of the Agreement on Agriculture. (See also paragraph 4.59 below).

4.57 Referring to the European Communities’ arguments summarized in paragraph 4.46, the Complainants submitted that the provider of the export subsidy was the European Communities itself, because there were "payments on the export of an agricultural product that are financed by virtue of governmental action" within the meaning of Article 9.1(c). The European Communities itself, not its sugar producers, took the governmental action that financed the payments, thereby giving rise to the subsidy. The EC producers were the recipients of the subsidy, in that they could increase their net income by making sales of C sugar at prices well below the cost of production. The EC producers, in turn, also made the "payments" when selling the C sugar to the world market buyer at prices below total cost. But this was irrelevant as "the payment could be made by private parties." According to Article 1 of the SCM Agreement, however, a "subsidy" could only be provided by a government, or at government direction.

4.58 The Complainants submitted further that the "subsidy" was conferred by the "payments financed by virtue of governmental action", and that the European Communities had erred in assimilating the concept of "payment" with the broader concept of "subsidy". In their view, the "payment" was only one element of a "subsidy" as defined in Article 9.1(c). Nothing in the text of Article 9.1(c), or in the Appellate Body's interpretation thereof, suggested that the recipient of the payment was, or needed to be, the same person that received the subsidy. The payment could be made by, or to, a private party. Moreover, it was well established that there could be more than one beneficiary of a subsidy, with one party being the beneficiary of a subsidy that was actually paid to another party. In the present case, the EC sugar producers received a subsidy notwithstanding the fact that the world market buyers of C sugar might also benefit. Citing the ruling of the Appellate Body in Canada – Dairy, the Complainants maintained that a payment could only be financed by virtue of a governmental action that conferred a benefit on the entity making the payment. However, for there to be a "payment" by the entity benefiting from that governmental action, it was not necessary that the benefits of that governmental action be transferred to the recipient of the payments.

4.59 The Complainants, referring to the European Communities' arguments with respect to "benefit" (see for instance paragraph 4.51) disagreed that the notion of "benefit", or the requirement that a benefit be "conferred" on the recipient of the payments, was a constituent element of Article 9.1(c). That word was not even reflected in the text of that provision. The Complainants recalled that the chapeau of Article 9.1 made clear that all the items listed in the subsections of that article constituted an "export subsidy." Because Article 9.1 stipulated that a payment within the meaning of Article 9.1(c) constituted an export subsidy, once the elements of Article 9.1(c) were satisfied, then for the purposes of the Agreement on Agriculture, there was no need to make any additional showing that the other elements of an export subsidy as defined under Article 1 of the SCM Agreement were also present. The Complainants also recalled that, in any case, under Article 10.3 of the Agreement on Agriculture, the burden was on the European Communities to show that it was not providing the benefit that it considered to be required under Article 9.1(c).

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73 Panel Report on Canada – Aircraft Credits and Guarantees, para. 7.229.
74 Appellate Body Report on Canada – Aircraft Credits and Guarantees, para. 93.
75 Ibid, para. 84.
4.60 The Complainants maintained that payments by private parties came within the definitional scope of Article 9.1(c). In this connection, they argued that the European Communities' argument that the "payment" must confer the benefit was based on the importation of a notion into Article 9.1(c) that could not logically be applied to payments by private parties. While a government may decide for non-economic reasons to sell a product on non-commercial terms, a private party would, in the normal course of business, make sales on conditions prevailing in the market, thus in a manner that did not confer a "benefit" on the recipient of the payment. If the European Communities were correct that only sales on terms conferring a benefit on the purchaser were regarded to be "payments" within the meaning of the Article 9.1(c), this provision would in practice not apply to payments by private parties. Therefore, yet again its purpose would be defeated.

4.61 In the Complainants' view, the European Communities' interpretation would also place undue emphasis on the recipients of the payment, requiring that they obtain an "advantage" or "benefit". The Complainants submitted that the European Communities' argument could not be reconciled with the jurisprudence of the Appellate Body relating to this issue. In Canada – Dairy, the panel had found that "[a] reading of Article 9.1(a) to the effect that a 'payment' exists only if a benefit is granted, is further mandated by the general context of this provision which includes Article 1 of the SCM Agreement..." [t]hat provision explicitly requires that a "benefit" be conferred for there to be a 'subsidy' under the SCM Agreement'. This reasoning was explicitly rejected by the Appellate Body, which noted that while "[t]he concept of 'benefit' is an integral part of the definition of 'subsidy' in Article 1.1 of the SCM Agreement..." the Panel used this term, not to assist in defining the term "direct subsidies" in Article 9.1(a) of the Agreement on Agriculture but to define the word "payment". This ruling was held to demonstrate that the Appellate Body did not consider the concept of benefit to be relevant for determining the existence of payments. It was also argued that the European Communities' position was inconsistent with the reasoning of the Appellate Body in Canada – Dairy (Article 21.5 I). In that case, the Appellate Body considered whether the sale of so-called "commercial export milk" ("CEM") to domestic milk processors at world market prices would constitute a "payment" within the meaning of Article 9.1(c). In the Complainants' opinion, it was clear that the Appellate Body considered that a sale of a product at a price below the average cost of production constituted a payment within the meaning of Article 9.1(c) even if the purchaser could have bought the product at the same price on the world market and the sale therefore did not confer on the purchaser a "benefit". As the Appellate Body pointed out, the crucial question for a panel applying Article 9.1(c) was whether export production had been given an advantage. If the losses that producers incurred as a result of export sales at prices below the average cost of production were financed by virtue of government action, then export production had been given an advantage. For the Complainants, it was obvious that a payment could only be "financed by virtue of a governmental action" where that governmental action conferred a benefit on the entity making the payment. However, for there to be a "payment" by the entity benefiting from that governmental action, it was not necessary that the benefits of that governmental action be transferred to the recipient of the payments.

4.62 The Complainants underlined that, in both the Canada – Dairy case and in the present case, the payers received an advantage as they were not charging prices which fully reflected their total production costs because of cross-subsidization of export production from quota production. In the same way, export production had been given an advantage. Further, as outlined in paragraph 4.58, the "subsidy" was not found in the "payment" itself, but in regard to the three elements comprising the export subsidy definition of Article 9.1(c), taken together, and by examining the losses made and the financing received by the entities making the "payment". In this connection, the Complainants underlined that there was no need to adopt a "recipient-oriented" approach to the determination of the payments, and thus no need to show a "benefit". The Complainants argued that, even though private...
parties could make the payments, it was the Member which was "responsible for ensuring that it respects its export subsidy commitments under the covered agreements".  

4.63 **Brazil** pointed out that EC sugar producers did, in any case, obtain a benefit from the Article 9.1(c) subsidies on the export of C sugar to the extent that those subsidies made profitable sales that were made well below the producers' total cost of production. Brazil considered that, as a factual matter, the European Communities had not disputed this benefit. Further, this benefit satisfied the requirements of Article 1.1(b) of the SCM Agreement.

4.64 In relation to the European Communities' contention regarding the appropriate benchmark in order to determine the existence of payments, the Complainants reiterated that the most appropriate benchmark in this case was the cost of production benchmark, for the reasons articulated by the Appellate Body in Canada – Dairy, and referred to in paragraph 4.38 above. As in Canada – Dairy, the domestic price was not appropriate because the intervention prices ensured it remained at artificially high levels. Similarly, the world market price did not provide a suitable benchmark because C sugar could only be sold at prices competitive with world market prices because it received export subsidies that made it competitive on that market. Applying the world market price as a benchmark would allow most subsidizing practices to escape the strictures of Article 9.1(c). The only subsidies that would be captured under that provision would be those designed to undercut the world market price. The Complainants noted that the European Communities provided no substantive reasons in support of its arguments and did not explain, in particular, why the factual differences between Canada – Dairy and the present case called for a different benchmark; why in the present circumstances, the cost of production benchmark could not serve as an appropriate test; and why the world market price was more appropriate in spite of the reasoning of the Appellate Body.  

In contrast, the Complainants highlighted that the Appellate Body in Canada – Dairy found that in circumstances "where the alleged payment is made by an independent economic operator and the domestic price is administered" the average cost of production represents the appropriate standard. As the factual circumstances in the present case were that the payments were also made by private operators and the domestic price was administered, the average cost of production was the appropriate benchmark.

4.65 The European Communities responded that the Canada – Dairy jurisprudence confirmed that the requirement to show an "advantage" or "benefit" was implicit in the requirement that there must be a "payment". The "crucial question" was whether the "payments" themselves conferred an "advantage" to the "export production", rather than to the foreign purchasers of that production. The European Communities stressed that the "payments" alleged in the present dispute did not transfer any "economic value" to the sugar producers and therefore did not confer any "advantage" to "export production". To the contrary, through those "payments", it was the sugar producers who transferred "economic value" to their foreign customers. The "actions" which, according to the Complainants, "financed" the "payments", constituted distinct measures from the alleged "payments" and were subject to specific disciplines under the Agreement on Agriculture, since some of those actions were not subsidies (e.g. the tariff protection), while others involved subsidies (e.g. the intervention purchases), but were not export contingent. Even assuming that the exports of C sugar involved "payments", the European Communities continued, such "payments" would not confer a subsidy on exports of C sugar.

4.66 Even if Article 9.1(c) did not use the term "benefit", the European Communities considered that all the measures listed under Article 9.1 were described as "export subsidies" in the chapeau of that provision. They had, therefore, to be interpreted in the context of the notion of "subsidy". The  

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existence of a "benefit" was inherent in the notion of "subsidy". Consequently, if the exports of a given agricultural product received no benefit from a certain measure, these products could not be deemed "subsidized" by such a measure.

4.67 The European Communities submitted that its reading of Article 9.1(c) and of Canada – Dairy as addressing exclusively the supply of inputs within the exporting country, was supported contextually both by the SCM Agreement, as confirmed by the Appellate Body\(^{80}\), and by the Members' schedules. The European Communities held that the definition of a subsidy in the SCM Agreement envisaged the existence of a subsidy without a "financial contribution"\(^{81}\) or in circumstances where the "financial contribution" was made by a private party rather than by a government, similar to Article 9.1(c).\(^{82}\) In contrast, Article 1 of the SCM Agreement always required, as an indispensable element for the existence of a subsidy, the conferral of a "benefit"\(^{83}\), and provided no exception to this requirement. Furthermore, under the SCM Agreement, the provision of goods by the government or by a private party, in the circumstances described in Article 1.1(a)(1)(iv), could constitute a subsidy if it conferred a benefit to the enterprise receiving such goods. The existence of a benefit had thus to be determined in relation to prevailing market conditions in the country of provision or purchase\(^{84}\) or, in the case of export subsidies, in the world market.\(^{85}\) On the other hand, under the SCM Agreement, the mere fact of exporting goods at "too low" a price had never been considered a subsidy, let alone an export subsidy, regardless of the benchmark.

4.68 The European Communities thus considered that the solution reached by the Appellate Body in Canada – Dairy was in line with the applicable rules of the SCM Agreement with respect to input subsidies, except that the Appellate Body took the view that, in certain circumstances, the existence of a subsidy had to be established in relation to a cost of production benchmark, rather than to a domestic market or world market price benchmark. The European Communities saw no apparent reason why agricultural products should be subject to stricter disciplines on export subsidies than other products. Recalling that the starting point for the negotiation of the rules on subsidies included in the Agreement on Agriculture was Article XVI of the GATT 1947, which only prohibited export subsidies on non-primary products, the European Communities asserted that the intention of the drafters of the Agreement on Agriculture was rather the opposite.

4.69 With regard to the Members' Schedules, the European Communities noted that the schedules of reduction commitments were part of the WTO Agreement and, as such, relevant context for the interpretation of Article 9.1(c) of the Agreement on Agriculture. The European Communities reasoned that, if the Complainants' interpretation of Article 9.1(c) were correct, those Members, which prior to the conclusion of the WTO Agreement provided export subsidies covered by the Complainant's interpretation, should have been expected to schedule reduction commitments with respect to those measures. Yet, not a single WTO Member did so, even though many of them applied, and continued to apply, price support measures (or tariff protection) having the effect of "cross-subsidizing" exports at below cost of production. In the European Communities' view, this demonstrated that the interpretation of Article 9.1(c) advanced by the Complainants was not envisaged by any Member, including the Complainants themselves, and would have, if upheld, far-reaching and unintended implications, including for developing countries. In support of this argument, the European Communities referred to documentation suggesting that a number of

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\(^{81}\) Article 1.1(a)(2) of the SCM Agreement.

\(^{82}\) Ibid., Article 1.1(a)(1)(iv).

\(^{83}\) Ibid., Article 1.1(b).

\(^{84}\) Article 14(d) of the SCM Agreement.

\(^{85}\) Item (d) of the Illustrative List of Export Subsidies in Annex I of the SCM Agreement.
countries, including Australia, Brazil, and Thailand, had been exporting sugar at a loss for years, and applying measures to keep domestic prices above world market prices.86 87

(b) "Financed by virtue of governmental action"

4.70 The Complainants submitted that there was a strong demonstrable link between the "payments" and the "governmental action" in the present case and referred to an assessment by the EC Commission88 suggesting that full liberalization of the EC sugar market would lead to a reduction in EC production of sugar to one third of present levels and even to its disappearance in the long run, and that profitability was only maintained through the EC sugar regime. The Complainants inferred that, under such circumstances, sugar production, including C sugar, in the European Communities depended on governmental action for its existence.

4.71 The Complainants recalled that the EC sugar regime regulated C sugar production and exports through Council Regulation No. 1260/2001. The funding of the payments that C sugar producers were making was the direct consequence of the extremely tight regulatory framework set out in that Regulation, under which quota holders were accorded the exclusive rights to make sales at guaranteed prices covering all or most of their fixed costs of production. The European Communities had created a legal framework that encouraged overproduction, segregated the export market for C sugar from the domestic market, generated the profits used to fund the export of that sugar, and imposed sanctions for failure to export such sugar. The EC Commission itself regarded the regime as a factor of market balance89, fulfilling market stabilization objectives.90 According to the Complainants, the governmental action involved in the EC sugar regime represented therefore a strong nexus with the 'payments', sufficient to meet the Appellate Body's test established in Canada – Dairy.

4.72 The Complainants asserted that the instruments of the regime provided a strong incentive to EC quota holders to defend their quotas through surplus C sugar production, whether or not the production of C sugar would be below the costs of its production. A quota value was delivered to a sugar quota holder through a combination of the EC system of subsidies and domestic supply restrictions. The intervention price provided a guaranteed price some three times greater than the world price, but due to the domestic supply restrictions, quota holders secured market prices substantially in excess of the intervention price. They also received export subsidies for quota quantities in excess of domestic supply needs. As there had not been any intervention purchasing for around 25 years, subsidized exports were obviously more profitable than selling into intervention. Given that high costs of production made EC sugar processors uncompetitive by world market standards, the quota value was directly attributable to the governmental action prescribed in the EC regime.

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86 Exhibit EC-21. See also Exhibit EC-17, pp. 27-30; Exhibit EC-18, p. 2; Exhibit EC-20, pp. 1-4; Exhibits EC-22 and EC-23; Exhibit EC-19.
87 At the interim review, Australia recalled that the Complainants strongly rebutted the European Communities’ position, arguing that to assert an equivalence between the EC regime and the sugar policies of other exporters ignored the elements of the EC regime which made it WTO-inconsistent. Specifically, the exceptionally high level of EC support, the delivery of that support through quotas for sales on the domestic market, the restrictions on carryover of C sugar and the requirement that C sugar not carried over be exported. These elements of the EC regime drove the production and export of subsidized C sugar and distinguished it from other regimes. The Complainants noted that the European Communities had failed to respond to the other arguments on "payments" raised by the Complainants and hence the European Communities had not met its burden of proof on these issues under Article 10.3 of the Agreement on Agriculture.
88 Exhibit COMP-6, p. 33.
89 Exhibit COMP-6, p. 34.
The Complainants sustained that beneficiaries of sugar production quotas were protected from virtually all foreign sources of competition, through a combination of import tariffs and special safeguard measures, and through the exportation, with export refunds, of a quantity of sugar allegedly "equivalent" to the quantity imported from the ACP countries and India. They were also protected from potential competition from new domestic suppliers because only sugar produced by holders of production quota was entitled to receive price support and export refunds. As a result, there was no competition between domestic sugar quota holders, and no re-allocation of quotas to the more efficient domestic producers. The level of the intervention prices covered the production costs of the least efficient sugar producer with the consequence that the more efficient producers enjoyed, what the staff of the EC Commission described as, "comfortable margins."  

The Complainants contended that, as in Canada – Dairy, this controlling governmental action was "indispensable" to the transfer of resources from consumers and tax payers to sugar processors for A and B quota sugar and, through them, to growers for A and B quota beet. The European Communities' action thereby financed growers to supply beet for C sugar to processors at prices that did not reflect the average total cost of the beet, and for those processors, in turn, to provide C sugar to buyers at world market prices that did not reflect its average total cost. EC sugar producers were thus able to recover most or all of their fixed costs by producing and selling quota sugar either in the protected domestic market or, with export refunds, in the world market. EC producers could then produce and export C sugar profitably as long as the world market price was higher than the marginal cost of producing C sugar. The Complainants argued that allocation of the right to supply the EC domestic market cross-subsidized sales of C sugar that otherwise would not be made, or would be made at a loss. They maintained that there was a single line of sugar production, for all sugar, irrespective of the destination markets. The same was true, mutatis mutandis, for sugar beet. The higher revenue sales for quota sugar in the internal market effectively financed some or all of the costs of C sugar. C sugar was cross-subsidized through direct subsidies, price support mechanisms and related mechanisms for quota sugar, all of which were regulatory instruments of the EC sugar regime. The sales of C sugar were profitable at prices that merely exceeded marginal costs because the higher revenue sales in the internal market "effectively 'financed' part of the lower revenue sales by funding the portion of the shared fixed costs attributable to the lower priced products." Again, the same was true, mutatis mutandis, for sugar beet. In the Complainants' view, this provided further evidence of the "demonstrable " link between the government action and the payment. Further, the Complainants argued that the structure of support through quotas and restrictions on quota trade and carryover of C sugar provided a particularly strong quota insurance reason for C sugar production. The Complainants asserted that, if the producer had a choice to either sell on the EC domestic market or on the world market, the former would be more attractive, given that the EC regime delivered a domestic price of some 3.5 times the world price of A quota sugar and 2.5 times that of B quota sugar.

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91 Exhibit COMP-6, p. 12.
92 Appellate Body Report on Canada – Dairy, para. 120.
93 Exhibit COMP-2, p. 121.
94 Exhibit ALA-1, p. 31. See also Exhibit COMP-2, p. 117.
95 Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US II), paras. 139-140.
96 Exhibit ALA-1, pp. 25-27.
4.76 The Complainants considered that the distinction between domestic support and export subsidies in the Agreement on Agriculture would be eroded if a WTO Member were entitled to use domestic support without limit to subsidize the exports of agricultural products. The benefits intended to accrue through a WTO Member's export subsidy commitments would thus be undermined. This rationale applied to the EC sugar industry, including both growers and processors who disposed of C beet and C sugar at prices that did not recover their total costs of production. The provision of domestic support measures coupled with high levels of tariff protection allowed extensive support to producers, inconsistent with the limitations imposed through the export subsidy disciplines.

4.77 The Complainants contended that C sugar exports were not incidental to the manufacture and sale of quota sugar as these amounted to between *** per cent and *** per cent of quota production between the 1992/93 and 2001/02 marketing years. The share of C sugar in production and exports demonstrated that C sugar was thus not a mere "spill over" of quota production, but a significant structural component of EC sugar production. As EC sugar production was dependent on governmental action for its very existence, there was clearly a demonstrable link between the payment and the governmental action sufficient to meet the tests established by the Appellate Body. The regulation of the EC regime, in the form of guaranteed prices for quota sugar and the forced export of over-quota production, the Complainants continued, underscored this governmental action. The maintenance of C sugar production and exports in the face of the high difference between production costs and prices received was only made possible by the subsidies on quota sugar and sugar processed from imported raw cane sugar and because of the absence of controls in the EC regime to prevent cross-subsidization. Australia noted that, with respect to subsidies for processing, competition from imports was effectively neutralized in regard to the guaranteed prices for some imported sugar, equating to the domestic support price for quota sugar. The Complainants reiterated that there was thus a "payment" which had been financed "by virtue of governmental action".

4.78 The European Communities responded that even if the domestic support provided to A and B quota sugar had the incidental effect of "financing" or "cross-subsidizing" exports of C sugar, this would not be sufficient to consider that those exports benefited from "export subsidies" subject to reduction commitments under the Agreement on Agriculture. The relevant question was not whether exports of C sugar were contingent upon subsidization, but instead whether the subsidies provided by the European Communities were contingent upon such exports. The European Communities considered that the Complainants had not alleged, let alone proven, that the measures which, according to them, "financed" or "cross-subsidized" the exports of C sugar were contingent, i.e. "conditional", "dependent for their existence" on the exports of C sugar.

4.79 The European Communities noted that some of the measures cited by the Complainants, such as import tariffs or safeguard measures (see for instance paragraph 4.73) , were not even subsidies. Other measures, such as the intervention price and the production quotas, were indeed typical domestic price support mechanisms, and were already subject to the European Communities' domestic support reduction commitments under the Agreement on Agriculture. Therefore, the question of whether these measures provided export subsidies to C sugar did not even arise, in the European Communities' opinion. Even if these measures provided an indirect benefit to C sugar, they were not contingent upon the export of C sugar and, therefore, could not be characterized as "export subsidies". The European Communities explained that a sugar producer's eligibility for A and B production quotas did not depend on whether it exported any sugar. Likewise, the right to sell A and B sugar into intervention was not conditional upon whether it exported C sugar or indeed any sugar at all.

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98 Exhibit ALA-1, p. 5.
4.80 In relation to the Complainants' assertions in paragraph 4.77, the European Communities observed that the volume of C sugar production fluctuated considerably from one marketing year to another, due to weather conditions, which affected both the beet yield and the sugar content of the beet, and to the evolution of the world market prices for sugar.¹⁰⁰ Sugar producers were free to decide whether or not to produce C sugar for export. The European Communities submitted that, far from requiring the exportation of C sugar, the EC regulations provided for the possibility to store and "carry forward" to the next marketing year any sugar produced in excess of the A and B quotas up to an amount equivalent to 20 per cent of the A quota (see also paragraph 4.48).¹⁰¹

4.81 The Complainants responded that the European Communities' arguments in paragraphs 4.78 and 4.79 disregarded the fact that any type of governmental action financing payments on exports of agricultural products was covered by Article 9.1(c).¹⁰² There could be no doubts therefore that the governmental action financing the payments could take the form of import tariffs, safeguard actions and other measures that would not constitute subsidies within the meaning of Article 1 of the SCM Agreement.

4.82 The European Communities also incorrectly ascribed a test to Article 9.1(c) requiring that the financing it provided to C sugar exports be contingent on such exports. In doing so, the European Communities was shrinking the export subsidy definition of that provision into one single element, thus implying that the governmental action constituted the subsidy. The terms of Article 9.1(c) clearly linked the requirement of export contingency to the "payments", not to the "governmental action" by virtue of which they were financed.¹⁰³ Hence, in order for the "payment on the export", including that made by a private party, to constitute an export subsidy in accordance with Article 9.1(c), such a payment had to be financed "by virtue of governmental action", with the requisite nexus existing between both elements.¹⁰⁴ The Complainants thus considered that the "demonstrable link" and "clear nexus" between the "payments" and the "governmental action" was well established in this case.

4.83 The Complainants submitted that it was this additional requirement which prevented Article 9.1(c) from becoming a per se anti-dumping rule, as advanced by the European Communities (see paragraph 4.51), and distinguished the subsidization defined in Article 9.1(c) from the kind of price discrimination by private actors with which anti-dumping instruments were concerned. In response to the European Communities' argument that the Complainants' interpretation would transform Article 9.1(c) into a provision prohibiting dumping by private operators, it was argued that Members would not be made responsible for export transactions by private operators that escaped their control. This was because there could only be an export subsidy within the meaning of Article 9.1(c) if there were (i) "payments" (ii) "on the export" (iii) "financed by virtue of governmental action". As to "payments", the Appellate Body stated that the government "must play a sufficiently important part in the process by which a private party funds 'payments', such that the requisite nexus exists between 'governmental action' and 'financing". It was thus clear that only payments which were directly linked to a governmental action were covered by Article 9.1(c). As to the requirement that the payments be "on the export", the Canada – Dairy panel correctly concluded that there was a payment "on the export" only if the Member caused it to be a payment contingent upon export performance. In the Complainants' view, the mere fact that private persons decided to export products below the average total cost of production was consequently not sufficient to establish export contingency. Finally, not any "financing" was covered by Article 9.1(c) but only financing

¹⁰⁰ Exhibit COMP-2, pp. 117-121.
¹⁰¹ Article 14 of Regulation No. 1260/2001; and Article 2(1) of Commission Regulation (EEC) No. 65/82.
that resulted from a governmental action. Each of the three elements constituting an export subsidy within the meaning of Article 9.1(c) was thus present only if the Member, not private operators, caused it to be present.

4.84 The Complainants held that the inconsistency of the C sugar regime was attributable to numerous governmental decisions. In particular, the Complainants noted that: first, the European Communities had decided to provide price support to sugar producers, thereby "financing" the "payments on the export" of C sugar; second, the European Communities had chosen to deliver that support through a set of shares in quota access to the domestic market, third; third, the European Communities had decided to permit (and encourage) producers to sell an amount of sugar that exceeded the amount of that quota, which – together with a series of other measures – had created the requisite nexus between the "payments" and the "governmental action" by virtue of which they were financed; and, fourth, the European Communities had decided to require producers to sell the excess amount of sugar on the world market, thereby ensuring that all payments were "on the export" of C sugar. The presence of all three elements constituting an export subsidy within the meaning of Article 9.1(c) was thus the direct and foreseeable consequence of actions by the European Communities, not merely the decisions of private sugar producers responding to market incentives.

4.85 The European Communities responded that an "advantage" had to be conferred by the "payment", i.e. by the provision of goods, rather than by the measures that "financed" the "payment", consistently with the definition of a "subsidy" in the SCM Agreement, which required that the "benefit" had to be conferred by the "financial contribution". The European Communities held that in the present case, the "financial contribution" would be the exports of C sugar. Accordingly, it was those exports which would need to provide a "benefit" to the sugar producers. In the European Communities' opinion, the Complainants were combining two of the three requirements of Article 9.1(c), i.e. the requirement that there must be a "payment" and the requirement that such "payment" be "financed by virtue of governmental action". The European Communities reiterated that the existence of an "advantage" was necessary in order to establish that there was a "payment". If there was no "payment", the subsequent question of how such "payment" was financed did not even arise. Consequently, the Complainants could not rely on the actions that supposedly financed the "payments" in order to conclude that there was a "payment". Rather, they should have demonstrated first that there was a "payment".

4.86 The European Communities submitted that, from the fact that a party had derived an "advantage" from certain "governmental actions", it did not follow necessarily that any provision of goods made by that party would "transfer economic resources" to the recipient of the goods. The European Communities was not saying that the "governmental action" referred to in Article 9.1(c) might never provide a "benefit" to the producers of exported goods. Rather, the European Communities' contention was that the "benefit" had to be examined on its own merits, and under the relevant WTO rules. It was essential to maintain this distinction because the notion of "governmental action" encompassed a very broad range of measures, including measures that were not subsidies (e.g. import duties). In the European Communities' view, by de-linking the "benefit" from the "payment" and attaching it to the "governmental action", the Complainants' interpretation of Article 9.1(c) would extend the application of the strict rules on export subsidies provided in the Agreement on Agriculture to virtually any form of government intervention which might have the incidental effect of "financing" sales at a loss. According to the European Communities, this was never intended by the drafters of the Agreement on Agriculture.

(c) "payment on the export"

4.87 The Complainants contended that the payments made by C sugar producers were payments "on the export" of "an agricultural product" within the meaning of Article 9.1(c). C sugar was included in Annex I of the Agreement on Agriculture and was therefore an agricultural product within
the meaning of that Agreement. Further, C sugar could only be sold upon its exportation: if not
carried forward, C sugar "may not be disposed of on the Community's internal market and must be
exported without further processing." Because of that legal requirement, the Complainants
considered that subsidies to C sugar, which must be exported, were subsidies "on the export" of that
product. Similarly, because C beet could be processed only into C sugar, a product that had to be
exported, payments to growers of C beet were also payments "on the export" of that product.

4.88 The European Communities responded that the alleged "payments" took the form of
exports, but were not made on "exports." The requirement of "contingent upon export performance"
set out in the Agreement on Agriculture had to be read in the same way as the same requirement
imposed by the SCM Agreement. Unlike in Canada – Dairy, the making of the alleged "payments"
was not conditional on any exports being made by the recipient of the payments or by a third party.
By ignoring this difference, the Complainants' interpretation of Article 9.1(c) collapsed two distinct
legal requirements, i.e., the existence of "payments", and the existence of "exports", with the former
action being contingent upon the second. Combining the two requirements made it possible to
characterize as "export subsidies" payments which were not conditional upon exports. In the
European Communities' view, this amounted to saying that the alleged "payments" were contingent
upon themselves, which would render the second legal requirement, "on exports", redundant. Such
interpretation also confused the distinction between the disciplines on domestic support, export
subsidies and market access, a distinction which was, in the European Communities' opinion, a
fundamental feature of the Agreement on Agriculture.

4.89 From the domestic support perspective, the European Communities continued, the
Complainants' interpretation would imply that, whenever a system of price support had the incidental
effect of financing exports below average total cost of production, the Member concerned would be
required, in order to avoid a breach of its export subsidy commitments, to dismantle that system of
price support, even if such a system was fully in conformity with the relevant provisions of the
Agreement on Agriculture concerning domestic support. If a subsidy were export contingent, the
European Communities continued, it should be possible, at least in theory, to remove the condition
which made it export contingent, while maintaining the subsidy. If an alleged export subsidy could
not be withdrawn except by withdrawing a legitimate system of domestic price support, it was
because, according to the European Communities, it was not contingent "on exports".

4.90 With respect to market access, the European Communities recalled that the terms
"governmental action" in Article 9.1(c) encompassed a broad range of governmental measures,
including import tariffs. The Complainants' interpretation would imply that, if high import duties
had the incidental effect of "cross-financing" exports below the average total cost of production, the
Member concerned would have no alternative but to lower its import duty levels, even if such duties
were within that Member's tariff bindings. The European Communities reiterated that the domestic
support for A and B sugar was not contingent upon exports of C sugar which was demonstrated by the
fact that some sugar producers did not produce any C sugar at all. The European Communities noted
that according to data for the most recent marketing year, there were no exports of C sugar from Italy,
Greece and Portugal, while exports from Finland, Spain and Belgium/Luxemburg represented only a
fraction of their total sugar output.

4.91 The Complainants responded that the European Communities incorrectly ascribed to them an
interpretation that the "payments themselves" were "exports" and considered that the sole argument in
that regard rested on the assertion that domestic support could not form part of export subsidization.

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Having rebutted such argument in paragraphs 4.55, 4.59 and 4.82 above, the Complainants disagreed that they were required to establish that the domestic support provided to sugar producers was contingent on exports of C sugar. As shown by the Complainants, since C sugar had to be exported, all sales of C sugar constituted sales for export. Conversely, if C sugar were not required to be exported, there would be no payment on C sugar. Thus, a payment occurred only when C sugar was exported.

Moreover, when interpreting the terms of Article 9.1(c) that defined export contingency, the Complainants considered that it was important to recall that that provision defined the obligations of Members, not those of private persons acting independently of their government. A payment could therefore be regarded as a payment "on the export" only if the Member caused it to be a payment on the export. The mere fact that private persons decided to export products below the average cost of production was consequently not sufficient to establish export contingency. In the present case, the European Communities had adopted a regulation that required the export of all C sugar. Sugar producers were free to decide whether or not to produce C sugar but they were not free to decide whether to sell that sugar for domestic consumption or for export. The export contingency was thus the result of a measure taken by the European Communities.

Australia submitted that C sugar exports were a significant structural component of EC sugar production, with C sugar exports fluctuating around 17 per cent of the combined A and B quota for the European Communities during the decade to 2001-02. Also, production of C beet and C sugar was due in part to the need for producers to ensure their quota receipts, and in part to the profits derived from A and B sugar and the consequent profits made on the marginal production costs of C sugar. In Australia's view, beet and sugar producers did not decide to produce and export C sugar through market based decisions.

The Complainants concurred with the EC Commission's reference to the EC sugar regime as "a factor of market balance, fulfilling the market stabilization objectives of the sugar regime" (see also paragraph 4.71 above.) and considered that this was relevant, not only in regard to the requirement that the payments be made "by virtue of governmental action", but also in regard to the requirement that payments be made "on the export". In their view, the payments to C sugar, which had already been shown by the Complainants to be made "by virtue of governmental action", were made on the export because they were contingent and dependent on C sugar being exported.

The Complainants disagreed that their interpretation would have the consequence that Members would be required to dismantle their price support systems whenever these had the incidental effect of financing exports below average total cost of production. Such an effect, by itself, did not give rise to an export subsidy within the meaning of Article 9.1(c). The payments financed by such programmes had also to be contingent upon export performance. The Complainants recalled that in Canada – Dairy, the panel had noted that the mere existence of parallel markets for domestic use and for export with different prices did not necessarily constitute an export subsidy within the meaning of Article 9.1. Consequently, the mere existence of a domestic and an export market with different prices, and spill-over effects, from one to the other did not constitute an export subsidy within the meaning of Article 9.1(c). It was thus not the effect of cross-subsidization resulting from the decisions of private operators, by itself, that rendered the European Communities' scheme of domestic support inconsistent with Article 9.1(c).

There were many options available to the European Communities to deliver support in accordance with the Agreement on Agriculture, including the possible removal of the contingency element, while maintaining the underlying subsidy. In the present case, the Complainants suggested

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109 Exhibit ALA-1, p. 5.
that the European Communities could repeal the requirement that C sugar be exported and permit C sugar to be sold in the domestic market or introduce changes requiring that any sugar produced in excess of any year's quota be carried over to the next year's quota. The sugar regime was the only EC regime governing an agricultural product that required excess production to be exported. **Thailand** stressed in this connection that the CMO for sugar was the only CMO of the European Communities that permitted (and indeed encouraged) producers to exceed their production quotas and required them to export the surplus. **Thailand**'s interpretation of Article 9.1(c) would therefore not require the European Communities to do anything that it was not already doing in the field of agriculture. If the European Communities were to align its sugar policies to those followed in other agricultural sectors, it would ensure their consistency with Article 9.1(c). According to the **Complainants**, this also suggested that the European Communities was fully capable of devising means to provide permissible domestic support without allowing this support, in the words of the Appellate Body, to produce "spill-over economic benefits for export production." **111** The Complainants noted in this regard that the Appellate Body had specifically stated in **Canada – Dairy** that an appropriate benchmark in determining whether ‘payments’ existed under Article 9.1(c) should respect the separation between export subsidy and domestic support disciplines. The Appellate Body had stated that if domestic support could be used, without limit, to provide support to exports, it would undermine the benefits intended to accrue through a Member's export subsidy commitments.

4.97 The **European Communities** responded that if it permitted sales of C sugar in the EC market, those sales would depress the prices within the EC internal market, thereby undermining the level of domestic price support. Further, they would not be made at below the average total cost of production, but rather at the supported price prevailing within the EC market. In the European Communities' view, therefore, those sales would not involve "payments". In order to withdraw the alleged "export contingency", the European Communities would have no option but to eliminate the price differential between its domestic market and the export market, which was the very essence of any system of domestic price support. Removing the "export contingency" element by preventing exports of C sugar would amount, in the European Communities' opinion, to withdrawing the subsidy, since the alleged subsidies were the "payments" and not the domestic support and other measures that, according to the Complainants, financed the "payments".

4.98 Furthermore, the European Communities maintained that the Complainants' interpretation would introduce an unjustified difference in treatment between two equally legitimate forms of domestic support: price support (including price support resulting from tariff protection) and income support linked to production (e.g. through "deficiency payments" equal to the difference between the market price and a target price). In the European Communities' opinion, both systems of domestic support were just as apt to "finance" exports below cost of production. Yet, on the Complainants' interpretation, such exports would be prohibited only if they were "financed" by a system of price support, or by tariff protection, but not if they were "financed" by deficiency payments or a similar system. Any Member providing domestic price support or tariff protection would be required to put in place mechanisms to ensure that it made no exports below cost of production. In contrast, Members would be free to "finance" an unlimited quantity of exports below cost of production via "deficiency payments" or other systems of income support linked to production, because sales in the domestic market would also be made below cost. The Complainants' interpretation would alter the architecture of the **Agreement on Agriculture** by redrawing the agreed boundary between domestic support and export subsidies in a manner that no participant in the Uruguay Round negotiations could have anticipated. And it would introduce a totally unjustified difference in treatment between different forms of domestic support and, ultimately, between Members.

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2. In the alternative, Article 10.1 of the Agreement on Agriculture

4.99 Should the Panel decide that the exports of C sugar were not subsidized by payments financed by virtue of governmental action within the meaning of Article 9.1(c), the Complainants submitted, in the alternative, that the European Communities had to address their claims under Article 10.1. In this regard, they recalled that under Article 10.3 of the Agreement on Agriculture, the European Communities had the burden of establishing that sugar exported in excess of its quantity commitment level was not subsidized by way of export subsidies not listed in Article 9.1, and that this reversal of the burden of proof extended to establishing the absence of any export subsidy whether listed in Article 9.1 or not (See section IV.C, Burden of proof).

4.100 Referring to the Appellate Body finding in US-FSC, the Complainants continued, three elements had to be met under Article 10.1 of the Agreement on Agriculture, i.e. that: (a) there was a subsidy not identified in Article 9.1; (b) that subsidy was contingent on export; and (c) the subsidy resulted in, or threatened to lead to, circumvention of a Members’ export subsidy commitments (the “circumvention” element). Though the European Communities had the obligation to demonstrate that these elements were not present, the Complainants set out the following arguments for reasons of procedural efficiency, and without waiving their rights under Article 10.3 of the Agreement on Agriculture. The Complainants thus argued that the European Communities was applying an export subsidy of a type not listed in Article 9.1, in a manner which resulted in, or which threatened to lead to, circumvention of export subsidy commitments, inconsistently with Article 10.1.

4.101 The European Communities responded that certain issues brought by the Complainants under Article 10.1 of the Agreement on Agriculture actually constituted “claims” which were, in its view, outside the terms of reference of the Panel (see section I.1, Terms of reference). Alternatively, the European Communities submitted that exports of C sugar did not benefit from any “other export subsidies” within the meaning of Article 10.1 of the Agreement on Agriculture.

(a) Item (d) of the Illustrative List of Export Subsidies

4.102 The Complainants submitted that Item (d) of the Illustrative List of Export Subsidies in Annex I of the SCM Agreement was clearly applicable to the present case. They specifically referred to the analysis of the panel in Canada – Dairy setting out the three elements which needed to be established:

(a) the provision of products for use in export production on terms more favourable than for provision of like products for use in domestic production;

(b) by governments either directly or indirectly through government mandated schemes; and

(c) on terms more favourable than those commercially available on world markets.

4.103 With respect to the first element, the Complainants submitted that, physically, C beet was identical to A and B quota beet, and had the same end use as an input into a manufacturing process. The three classes of beet were thus “like products”. However, the regime provided for the supply of C beet and quota beet to processors on different terms. First, C beet could not be processed into sugar

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for sale on the domestic market, and thus most C beet was processed into C sugar for export. All C sugar must be exported without an export refund. Conversely, most sugar on the domestic market was quota sugar, processed from A and B beet. Second, while growers were guaranteed a fixed minimum price for quota beet, no fixed price was set for C beet, the Regulation permitting the provision of C beet at a lower price than quota beet. While the price obtained for C beet was not uniform, as a general rule C beet was provided to processors on terms more favourable than those of A and B beet. Referring to the average prices, as did the panel in Canada – Dairy, products for export production, the Complainants continued, were being supplied for less than like products for domestic production. By controlling the disposal of C sugar, the European Communities limited the use to which C beet could be put and hence ensured that C beet was available at prices that were "more favourable" than the prices of A and B beet. According to the Complainants, the first element of Item (d) of the Illustrative List was therefore satisfied.

4.104 With respect to the second element, the Complainants noted its similarity to the "governmental action" component of Article 9.1(c) of the Agreement on Agriculture as both phrases denoted some level of governmental involvement in the subsidization of export products. However, the Complainants pointed out that the residual nature of Article 10.1 meant that it might cover export subsidies which did not satisfy some component of an Article 9.1 subsidy. Thus, this second element had been interpreted more broadly, according to the Complainants, than similar phrases in Article 9.1(a) and Article 9.1(c) of the Agreement on Agriculture. The Complainants submitted that should the Panel find that there was no 'governmental action' component under Article 9.1(c), this would not preclude a positive finding on the second element of Item (d) of the Illustrative list.

4.105 Turning to the substantive test of the second element, the Complainants recalled that the panel in Canada – Dairy had held that the prohibition on diversion of CEM back into the domestic regulated market and the exemption which gave processors for export access to the lower CEM prices were sufficient for a finding that the provision of milk was "made or mandated by government for export." They considered that these two factors were also present in the EC sugar regime as the European Communities exempted C beet from the minimum price requirement under Article 5 of the Regulation, while Article 13 of the Regulation operated to ensure that C beet could not be used to produce products that would obtain the higher regulated prices for sugar sold within the European Communities. Similarly, by exempting C beet from the minimum price requirement and preventing the use of C beet to produce sugar that could be placed on the domestic market, the European Communities mandated the provision of beet for C sugar exports on terms more favourable than would be available for beet used for the production of sugar for sale on the domestic market. The second element of Item (d) of the Illustrative List was therefore satisfied.

4.106 As concerns the third element, the Complainants considered that the focus of the third element was on the comparative attractiveness to exporters of sourcing products for export production from either the domestic market or from the world market, rather than specifically on the regulation of access to the world market. If the domestic market was a more attractive source than the world market, this element was established. Furthermore, the domestic product supplied on favourable terms for export production was beet. There was no world market for beet in commercial quantities, as beet was perishable and comparatively expensive to transport. Pointing to footnote 57 to Item (d)
of the Illustrative List, the Complainants held that, when comparing the attractiveness to exporters of sourcing beet from the EC domestic market or the world market, the former was necessarily more attractive to exporters as, for technical and other reasons (including protective tariffs against imports)\(^{123}\), commercial quantities of beet could not be acquired on the world market on any terms. The terms of domestic supply were thus inevitably more favourable, according to the Complainants. The third element of Item (d) of the Illustrative List was therefore satisfied.

4.107 Contending that they had established the three elements of Item (d) of the Illustrative List, the Complainants held that it was not necessary to consider whether the subsidies provided were "contingent upon export performance"\(^{124}\), as all measures within the Illustrative List were, by definition, contingent upon export performance. Recalling the Appellate Body's finding that the determination of 'export subsidies' under Article 10.1 of the Agreement on Agriculture should draw on the interpretation of that term under the SCM Agreement\(^{125}\), the Complainants argued that the export subsidy provided under the sugar regime thus fell within the terms of Article 10.1 of the Agreement on Agriculture. Under Article 10.1, the European Communities had the burden of establishing that its regime in respect of C beet was not an export subsidy to C sugar within the meaning of Item (d) of the Illustrative List.

4.108 Turning to the circumvention test, the Complainants recalled the jurisprudence in Canada – Dairy\(^{126}\) and in US – FSC\(^{127}\) and held that the appropriate test of circumvention was whether the European Communities was transferring economic resources to excess exports through methods other than those prohibited under Articles 3.3 and 9.1 of the Agreement on Agriculture. The Complainants observed that they had previously established (see paragraph 4.28 in Burden of proof) that the European Communities exported quantities of sugar in excess of the quantities specified in its reduction commitments. Having demonstrated that part of the excess quantity, C sugar, received an export subsidy within the meaning of Item (d) of Annex I of the SCM Agreement, or alternatively, within the meaning of Article 1.1 of the SCM Agreement, and having established the export contingency element, the Complainants submitted that the European Communities was circumventing its export subsidy commitments, inconsistently with Article 10.1 of the Agreement on Agriculture.

4.109 The European Communities responded that exports of C sugar did not benefit from export subsidies within the meaning of Item (d) of the Illustrative List and that this claim was unfounded. The relevant issue, in the European Communities' view, was whether the EC sugar regime mandated the provision of C sugar. From the fact that the EC sugar regime "mandated" minimum prices for A and B beet, it did not follow that the "provision" of C beet to the sugar producers was directly or indirectly "mandated" by the EC authorities. The European Communities reiterated that the beet farmers were entirely free to decide whether or not to produce C beet for export, and that the price of

\(^{123}\) According to the EC Schedule CXL, the bound rate on fresh sugar beet (HS 1212 91 91) was 67 ECU/tonne plus a special safeguard (SSG). The bound rate on dried or powdered sugar beet (HS 121291 20) was 230 ECU/tonne plus SSG. The bound rate on sugar cane (HS 1212 92 00) was 46 ECU/tonne plus SSG. Exhibit ALA-1, Table 3, for 2002/2003 indicative price: based on the WTO bound rates and sugar beet prices of €47.60/tonne for A quota and €28.84/tonne for C1 beet, the ad valorem equivalent of the above rates for fresh beet would currently be 140 per cent and 232 per cent respectively. For C2 prices (Table 3), the rate would be 676 per cent, plus the SSG; see also Taric database, Taric Code 1212918000, third country duty rate of €67/tonne. This figure did not include the special safeguards imposed on imports of sugar beet. (Note by the Secretariat: 1 ECU = 1 Euro).


the C beet was freely agreed between the growers and the sugar producers. In the European Communities' view, the absence of any element of government compulsion was confirmed by the fact that, in some member States, there was no production of either C beet or C sugar (see also paragraph 4.90).

4.110 The European Communities was of the view that the mere fact that a government measure enabled or promoted the provision of goods by private parties was not sufficient to consider that such action was "mandated" by the government. The interpretation of "mandated" found contextual support in the definition of "subsidy" included in Article 1 of the SCM Agreement, according to which the supply of goods to an enterprise could not be considered as a subsidy unless it was carried out by the government or by a public body. The only exception to this was provided in paragraph 1.1(a)(1)(iv). The European Communities recalled that the panel in US – Export Restraints, had rejected the claim by the United States that a restriction on exports of an input conferred a subsidy to the processors simply because it had the effect of making that input available at a lower price in the Canadian market. To the European Communities, the term "mandated" suggested a greater degree of government compulsion than the terms "entrust" or "direct". Since the EC authorities had not "explicitly and affirmatively delegated or commanded" the beet farmers to provide beet to the sugar producers for export, it was not providing goods indirectly through a "government-mandated scheme" within the meaning of Item (d) of the Illustrative List.

4.111 The European Communities contended that the Complainants' reasoning with respect to the term "mandated" and their reliance on the interpretation made by the panel in Canada – Dairy, disregarded the ordinary meaning of that term. According to the European Communities, that reasoning had been implicitly but unequivocally rejected by the Appellate Body in that same case, when it had emphasized that the terms "by virtue of governmental action" did not, unlike the term "mandated", involve any "compulsion". In the European Communities' opinion, therefore, Article 9.1(c) of the Agreement on Agriculture encompassed a broader range of government measures than Item (d) of the Illustrative List. Like the Canadian producers of CEM, the EC beet farmers were free to decide whether or not to produce C beet. Consequently, the measures at issue could not be characterized as "obligating", "driving" or "mandating" the beet farmers to "provide" additional beet for export.

4.112 The Complainants considered that the European Communities' argument in paragraph 4.109 was based on an interpretation of Item (d) of the Illustrative List which suggested that the export subsidy definition should be restricted to state trading operations. The relative freedom of a beet grower to grow C beet did not form part of the tests of Item (d). Instead, the tests related to whether the European Communities mandated the production of C beet to exporters on the same terms as beet sold on the domestic market, i.e. whether the beet farmer had the freedom to sell C beet to exporters on the same terms that he obtained for beet destined for the domestic sugar market. This was clearly not the case: C beet did not benefit from the fixed minimum price guarantee for quota beet and could not be used to produce sugar for sale on the domestic market.

(b) Article 1.1 of the SCM Agreement

4.113 Australia submitted, in the alternative, that if it were found that the EC regime did not provide an export subsidy under Item (d) of the Illustrative List, the European Communities still had to show that no other export subsidy was provided, according to the general definition of a subsidy in Article 1.1 of the SCM Agreement. Australia noted that, for the purpose of the SCM Agreement, a

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subsidy shall be deemed to exist if there was any form of income or price support in the sense of Article XVI of GATT 1994; and a benefit was thereby conferred.

4.114 With respect to the first requirement, Australia held that the EC regime was explicitly designed to provide income support for beet growers through the minimum price scheme previously outlined above (see for instance paragraphs 4.103 and 4.105.) The "chapeau" of Council Regulation No. 1260/2001\(^{131}\) described the objectives of the sugar regime as "to ensure that Community growers of sugar beet and sugar cane continued to benefit from the necessary guarantees in respect of employment and standards of living...". To achieve this, Australia continued, the regime provided for an intervention price which "...must be fixed at a level which will ensure a fair income for sugar-beet and sugar-cane producers...". The high import barriers and the existence of quota limits maintained the high price of sugar sold on the domestic market, and supported the income of growers and processors.

4.115 Australia noted that Article XVI of GATT 1994 included within its scope any income or price support "which operates directly or indirectly to increase exports of any product". According to Australia, the income guaranteed to EC growers and processors from the sale of quota sugar acted to counter any loss incurred on C sugar, in effect cross-subsidising C sugar exports. Moreover, the exclusion of C beet from the fixed minimum price required to be paid for quota beet allowed for its supply at a lower price, thus reducing the cost to the sugar processor. The fact that the price and income support were delivered through quota sugar was no barrier to the application of Article XVI, which governed measures acting "directly or indirectly to increase exports". Moreover, citing Article XVI:4, Australia noted that the EC regime obtained a price on the world market for C sugar which was lower than that obtained on the domestic market for A and B sugar. The regime therefore provided a subsidy within the definitional terms of Article XVI:4. Considering that Section B dealt with the export subsidy subset of the broader terms of Article XVI:1, Australia was of the view that the EC regime also provided a subsidy "which operated directly or indirectly to increase exports of any product." The EC sugar regime was therefore within the terms of Article 1.1(a)(2) of the SCM Agreement.

4.116 To constitute a subsidy under Article 1.1 of the SCM Agreement, Australia continued, it must further be shown that a benefit was conferred by the regime. According to Australia, the term 'benefit' under Article 1.1(b) of the SCM Agreement referred broadly to any "favourable or helpful factor or circumstance" afforded to the recipient of a measure under Article 1.1(a), and required a comparison between the situation of a recipient of this measure, and the situation of that recipient absent the measure.\(^{132}\) If the measure delivered any form of advantage to the recipient, the measure rendered a "benefit" under Article 1.1(b). Australia asserted that, in the present case, the provision as a whole referred to an advantage enjoyed by the recipients of income or price support under the EC regime, and that this advantage was readily identified. The price support given to quota beet and sugar, from which C beet and C sugar were excluded, allowed for the provision of beet for export sugar production at a lower price, thereby reducing the cost to the processor of producing export sugar. Further, the subsidies delivered through the high domestic price support level contributed to the offsetting of the cost of production, incurred by the sale of C sugar at the world market price. The definition of a subsidy under Article 1.1 of the SCM Agreement was therefore satisfied in Australia's view.

4.117 In order for this subsidy to fall within the terms of Article 10.1 of the Agreement on Agriculture, it had to be further established that the subsidy was an export subsidy. In this regard, Australia reiterated that C sugar was manufactured exclusively from C beet, and that C sugar must be

\(^{131}\) Chapeau para. (2) of Regulation No. 1260/2001.

exported (unless carried over). C beet was excluded from the fixed minimum prices required for A and B beet, conditional upon its not being used for quota sugar production. Therefore, the provision of C beet at lower cost for C sugar manufacture was conditional upon the exportation of C sugar. The regime therefore provided a subsidy contingent upon export performance.

4.118 The European Communities replied that the EC sugar regime provided price support to A and B sugar and to A and B beet, but not to C sugar or C beet. Moreover, the price support for A and B sugar and beet was not contingent upon exports of sugar and, therefore, did not constitute an export subsidy. There was no requirement to produce C sugar and, consequently, no requirement to export C sugar in order to benefit from the price support. Furthermore, the EC regulations allowed sugar produced above the A and B quotas, up to an amount equivalent to 20 per cent of the A quota, to be "carried forward". The European Communities further submitted that the definition of "export subsidy" found in Articles XVI.1 and XVI.3 of the GATT 1994 did not purport to define the notion of export subsidy. The European Communities considered that for the purpose of the Agreement on Agriculture, Article 1(e) defined the notion of "export subsidies" as 'subsidies contingent upon export performance'. A system of price or income support which "operates so as to increase exports" was not "contingent upon export performance" and could not be considered as an export subsidy for the purposes of the Agreement on Agriculture, regardless of its characterization under Article XVI. According to Australia's definition, virtually any form of domestic support would then have to be considered as an export subsidy.

4.119 Australia submitted that the European Communities' rebuttal was premised on the same, in its view, legally incorrect arguments that the European Communities had used in relation to Article 9.1(c) of the Agreement on Agriculture, i.e. that "contingency" must attach to the provision of price support, as compared to a "contingency" attached to "export." Australia underlined that Article XVI of GATT 1994 was not predicated on the subsidy being contingent on export. Rather, on the basis of a plain reading of Article XVI of GATT 1994, it was the operation of the income or price support in increasing exports that constituted a subsidy contingent on export performance.

4.120 Australia recalled that the export subsidy definitions in the SCM Agreement provided contextual guidance on the definition of an export subsidy for the purposes of Article 10.1 of the Agreement on Agriculture, as did Article 1.1 of the SCM Agreement, for the purposes of a definition of a "subsidy". Article 1.1(a)(2) made it clear that income or price support in the sense of Article XVI of GATT 1994 came within the scope of a subsidy definition. For the purposes of those export subsidies listed in the Illustrative List, the element of subsidization provided through price or income support formed part of an export subsidy in the circumstances described in Items (b), (d) and (l). Read in the context of Article 3.1(a) of the SCM Agreement, all subsidies included in the Illustrative List constituted 'subsidies contingent on export performance' in the circumstances defined in the respective items. According to Australia, therefore, the income or price support did not need to be provided exclusively for exports.

4.121 In this context, Australia considered that the Ad Note to Article XVI.3, paragraph 2 directly addressed the situation in regard to C sugar as arrangements involving: (a) "a system of price stabilization or of the return to domestic producers of a primary product independently of the movements of export prices"; (b) "which results in the sale of the product for export at a price lower than the price charged for the like product to buyers in the domestic market"; and (c) "where the operations of that system are wholly or partly financed out of government funds in addition to the funds collected from producers in respect of the product concerned." Australia held that Article XVI.4 of GATT 1994 would also capture such forms of subsidy, in circumstances where such subsidy resulted in the sale of a product for export at a price lower than the comparable price charged for the like product to buyers in the domestic market.
3. Good faith

(a) Exports of C sugar were consistent with the reduction commitments

4.122 The European Communities submitted that even if exports of C sugar were found to benefit from export subsidies, these would not exceed the reduction commitments scheduled by the European Communities, or would do so by much less than claimed by the Complainants. According to the European Communities, the Complainants' allegations failed to take into account the context provided by the Modalities Paper (see, for instance, paragraphs 4.37 and 4.143-4.145) as well as the requirements of the principle of good faith. By disregarding that the base quantity in the EC's Schedule did not include exports of C sugar, the Complainants' interpretation led to a result which was unfair because it would require the European Communities to reduce its exports by a much larger percentage (60 per cent) than that agreed in the Modalities Paper and applied by all other Members (21 per cent). In the European Communities' view, that result was not compatible with a good faith interpretation of its commitments.

4.123 The European Communities first recalled that its schedule of export subsidy reduction commitments was "an integral part" of the GATT 1994 and, therefore, of the WTO Agreement. As such, it had to be interpreted in accordance with the "customary rules of interpretation of public international law" embodied in Articles 31 and 32 of the Vienna Convention on the Law of Treaties ("Vienna Convention"). Noting that the "general rule of interpretation" set out in Article 31.1 of the Vienna Convention required interpreting treaty provisions "in good faith", the European Communities maintained that, even if the Modalities Paper was not part of the WTO Agreement, it was an agreement reached by all the participants in the Uruguay Round in connection with the conclusion of the Agreement on Agriculture. As such, it was relevant "context" for the interpretation of the schedules of reduction commitments, in accordance with Article 31.2(a) of the Vienna Convention.

4.124 The European Communities asserted that its schedule reflected the understanding that exports of C sugar did not benefit from export subsidies and that the Complainants were aware of this fact. The figure shown in the EC's Schedule LXXX under the heading "base quantity level" only included the exports of A and B sugar during the base period 1986-1990. The European Communities supplied statistical data showing that the total quantity of sugar exported from the European Communities during the base period was higher than the scheduled 1986-1990 base levels in EC Schedule LXXX. The figures that appeared under the heading "annual and final quantity commitment levels" were calculated from that "base quantity level" by applying the reduction percentage agreed in the Modalities Paper. Recalling its reasoning summarized in paragraphs 4.122 and 4.125, the European Communities concluded that the base quantity level would have been 3,188,200 tonnes instead of 1,612,000 tonnes, and the final commitment level would have been 2,514,700 tonnes (i.e. 79 per cent of 3,188,200 tonnes) instead of 1,273,500 tonnes (i.e. 79 per cent of 1,612,000 tonnes) if C sugar had been taken into account. Total exports of sugar during marketing year 2001/2002 were 2,443,600 tonnes (including exports of C sugar, and adjusted for ACP/India equivalent sugar which was, according to the European Communities, subject to a 1.6 million tonnes ceiling), i.e. 71,100 tonnes below the final commitment level as calculated above. The European Communities concluded that the breach of the European Communities' reduction commitments alleged by the Complainants would thus result exclusively from a scheduling error.

134 See Table 8 of the European Communities' first written submission; and Exhibit EC-9.
135 See Table 9 of the European Communities' first written submission.
4.125 The European Communities indicated that its reasoning was equally valid with respect to its budgetary outlay commitments. In other words, if the Panel found that the C sugar regime provided export subsidies, it would follow that the European Communities would have been required to include the amount of the export subsidies provided to exports of C sugar during the base period in the base outlay level from which the annual commitment levels were calculated, in accordance with the provisions of the Modalities Paper. According to the European Communities, the determination of that amount would require the calculation of the difference between the annual average total cost of production during each year of the base period and the actual prices of the export transactions made during that year. In this context, the European Communities indicated that Supporting Table 11 accompanying the EC Schedule LXXX specified that the amounts used in the calculation of the base outlay level for sugar were those of the producer levies collected on the production of A and B sugar during the base period and used to finance the refunds on exports of A and B sugar. No refunds were granted on exports of C sugar. It was clear, therefore, that the base outlay level scheduled by the European Communities did not include any outlay with respect to exports of C sugar.

4.126 The European Communities contended that, until recently, the Complainants had shared the understanding that exports of C sugar did not benefit from export subsidies and that exports of C sugar were not included in the scheduled base quantity and outlay levels. First, the C sugar regime had been in place since 1968 and was well-known to all the participants in the Uruguay Round and, in particular, to the Complainants, who were all major exporters of sugar. Before the Uruguay Round, Australia and Brazil had also challenged the European Communities' system of export subsidies for sugar but neither of them had raised any question. Similarly, during the Uruguay Round negotiations, no participant had made any suggestion that exports of C sugar benefited from export subsidies and should be subject to the reduction commitments, despite successive submissions, by the European Communities, of three draft schedules, followed by the verification process, which allowed the other participants ample opportunity, in the European Communities' opinion, to check the commitments. After the conclusion of the Uruguay Round, the European Communities asserted, official assessments conducted by Australia, the United States, and ISO, confirmed that shared understanding.

4.127 The European Communities submitted that the interpretation made by the Appellate Body in Canada – Dairy, on which the Complainants had principally based their allegations, was a novel one, which could not have been anticipated by any participant when the commitments were scheduled. The European Communities asserted that Article 9.1(c) was meant to address so-called "producer-financed subsidies" financed from the proceeds of production levies. Nothing in the drafting history of Article 9.1(c) suggested that the negotiators had in mind the European Communities' C sugar regime or, more generally, that they regarded the export of agricultural commodities below cost of

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136 Exhibit EC-4.
138 The European Communities indicated having submitted a first draft schedule of commitments on 16 December 1992 (Exhibit EC-4), a revised draft on 14 December 1993 (Exhibit EC-6), and a final version on 25 March 1994.
139 Appellate Body Report on EC – Computer Equipment, paras. 109-110. Tariff commitments "represent a common agreement among all Members" and "any clarification of the scope of tariff concessions that may be required during the negotiations is a task for all interested parties".
140 Exhibit EC-12, pp. 8 and 38. see also Exhibit EC-14, p. 37: ABARE confirmed that "production beyond the combined A and B quotas, called C sugar receives no price support" and that C sugar "is exported without support"; Exhibit EC-13 (the European Communities underlined that a distinction was established between "EC net exports" and "subsidized exports" in Table 1 on page 9).
141 Exhibit EC-15, p. 25.
production as an export subsidy. Also, three successive rulings by the Appellate Body on the same issues had been necessary to define the test on which the Complainants had relied in the present case. The European Communities contended that the interpretation eventually adopted had not been advanced by any of the parties during the proceedings and was strongly criticised by all of them, as well as by other Members, before the DSB on the grounds that it had no basis in the text of the Agreement on Agriculture.  

4.128 The European Communities underlined what it considered as fundamental differences between the present dispute and Canada – Dairy. First, the alleged violation of the scheduled commitments in Canada Dairy did not result from a scheduling error made during the negotiations, but rather from Canada's introduction, after the conclusion of the WTO Agreement, of a new regulatory regime. Secondly, the measures at issue in Canada – Dairy did not exist when the reduction commitments were negotiated, as they were not introduced by Canada until August 1995. Third, Canada had believed that the new regime would allow milk processors to increase their exports without breaching Canada's reduction commitments. Fourth, Canada did not contest that the regime in place during the base period, and up to 1995, conferred export subsidies, which was why Canada deemed it necessary to replace it. Fifth, Canada did not argue that the base level did not include all the subsidized exports made during the base period. For these reasons, the panel's finding in Canada Dairy that Canada had acted inconsistently with its reduction commitments did not require it to reduce its subsidized exports beyond the level agreed by the participants in the Uruguay Round. In contrast, the European Communities continued, the regime in the present case was in place at the time of the negotiations and indeed was the basis for the negotiated commitments. The European Communities, reiterating the points made in paragraphs 4.122-4.126, submitted in the alternative, that exports of C sugar should not be deemed to be in excess of the European Communities' reduction commitments, unless it was established (and, if so, only to that extent) that the quantity of subsidized exports exceeded the level of the final commitment that resulted from applying the reduction percentage agreed in the Modalities Paper to a base quantity which included exports of C sugar made during the base period.

4.129 Alternatively, should the Panel find that the C sugar regime provided export subsidies in excess of the reduction commitments, the only course of action consistent with the requirements of good faith would be for the Complainants to agree to the correction of the European Communities' scheduling commitments so as to include the exports of C sugar in the base levels and to rectify the annual commitments accordingly. Otherwise, the European Communities would be prejudiced, because it would be effectively required to reduce the quantity of subsidized exports by a much larger percentage than the one agreed to in the negotiations, namely by 60 per cent. Furthermore, if the footnote on ACP/India sugar were found to be invalid, the overall percentage of export subsidy reduction would be 73 per cent. (See also paragraphs 4.123-4.124) In this regard, the European Communities indicated that the possibility to correct errors in the text of a treaty was specifically envisaged in Article 79 of the Vienna Convention.

4.130 The Complainants responded that the issue before the Panel was the treaty text, i.e. the EC Schedule, which had to be interpreted in accordance with the customary rules of interpretation of public international law. Consequently, their alleged understandings during the Uruguay Round negotiations, as well as the verification process, were irrelevant as they were not part of the "context" under Article 31, nor "supplementary means of interpretation" under Article 32, of the Vienna Convention. In relation to the European Communities' contention in paragraphs 4.123-4.124, the Complainants submitted that Article 3.2 of the DSU made clear that recourse to the interpretative

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143 Exhibit EC-10, statements by Australia, New Zealand and the United States; and Exhibit EC-11, statement by Canada.
145 Ibid., paras. 4.279-4.280.
rules of the Vienna Convention were to be used to "clarify the existing provisions", and that dispute settlement must not add to or diminish rights and obligations provided in the covered agreements. Panels must follow the textual approach underlying the Vienna Convention rules and "interpretation was not a matter of revising treaties or of reading into them what they did not expressly or by necessary implication contain".¹⁴₆ The Complainants held that, rather than a good faith clarification, the European Communities was seeking from the Panel a revision of its Schedule, and a diversion from the ordinary meaning imparted from the Schedule’s text, and ultimately changing the figures in the EC Schedule by "interpreting" them. In their view, the figures indicated in the EC Schedule in respect of its export reduction commitments for sugar were unequivocal.

4.131 The Complainants rejected the characterization of the Modalities Paper as an "agreement" reached by all participants in the Uruguay Round. In their view, only the commitments undertaken under the Agreement on Agriculture were legally binding, which explained why that Agreement made no reference to the Modalities Paper. Recalling that the Modalities Paper was prepared during the latter stages of the negotiation of the Agreement on Agriculture, and not "on the occasion of the conclusion of the treaty" as required by Article 31.2 of the Vienna Convention, the Complainants held that the Modalities Paper did not provide "context" for the determination of the scope of subsidy reduction commitments in these proceedings because it was not an "agreement" relating to the Agreement on Agriculture, and because it was not accepted as an "instrument" made in connection with the conclusion of the Agreement on Agriculture.

4.132 The Complainants submitted that the intentions of the parties in the Uruguay Round should be taken into account when considering whether the Modalities Paper was context. These were explicitly reflected in the Note by the Chairman of the Negotiating Group on Market Access, which confirmed that the Modalities Paper was issued "for the purpose of completing draft Schedules of concessions and commitments in the agricultural negotiations and for facilitating the verification process leading to the establishment of formal Schedules to be annexed to the Uruguay Round Protocol" and "on the understanding of participants in the Uruguay Round that these negotiating modalities shall not be used as the basis for dispute settlement proceedings under the MTO Agreement". This meant that the Modalities Paper was not intended to provide any basis, interpretative or otherwise, for dispute settlement proceedings, and thus would not give rise to rights and obligations which could be the subject of dispute settlement proceedings, but was issued for a limited purpose, i.e. "completing draft schedules".

4.133 The Complainants acknowledged that the sole role the Modalities Paper could play in the interpretation of the Agreement on Agriculture and the associated schedules, was as "a supplementary means of interpretation", i.e. as an element of the "preparatory work" under Article 32 of the Vienna Convention. In that context, they considered that the Panel's discretion to look at the Modalities Paper as such was limited to "confirming" the meaning resulting from the interpretation of the EC's Schedule under Article 31 of the Vienna Convention. This limitation was due to the fact that the EC's Schedule was neither "ambiguous or obscure", nor led to "a result which was manifestly absurd or unreasonable" as required by the Vienna Convention (see also paragraph 4.130). Brazil added that, should the Modalities Paper be considered as "preparatory work", it should be accorded limited probative value, in light of the Chairman's Note.

4.134 The Complainants indicated that they became aware that exports of C sugar were made below cost of production and, therefore subsidized, only after the NEI report (see footnote 149) was issued in 2000.

4.135 **Australia** submitted that it did not have access to information that would have enabled it to make a definitive assessment that C sugar exports were being subsidized in the sense of Article 9.1(c) of the Agreement on Agriculture. It contended, however, that the European Communities had access to a wide range of information sources that would have enabled Australia to make an informed assessment of the cross subsidization of C sugar exports. The European Communities itself had identified a problem with C sugar since the EC Commission had proposed prohibiting the production of such sugar in 1973\(^{147}\), and knew, as far back as 1981, that the EC sugar regime resulted in the pooling of producers' receipts from sales in internal markets at supported prices.\(^{148}\) Australia noted that until late 2003, there was a marked absence of any published information undertaken by EC institutions on the economics of its sugar production and trade. Following an accumulation of evidence from European sources (including reports published or commissioned by the EC\(^{149}\)) and in light of the increase in C sugar exports from 1995 to 2000, Australia indicated that it was only then able to undertake independent detailed research which enabled it to challenge the European Communities' assertions that C sugar exports were not subsidized. In relation to the lack of reaction evoked by the European Communities (see paragraph 4.126), Australia referred to its letter of 10 December 1993 where it had registered its expectation that there should not be any exclusions from reduction commitments.\(^{150}\) The reference was not specific to C sugar and was primarily intended to register concerns about the European Communities' announced intent to exclude some sugar from its reduction commitments.

4.136 **Brazil** noted that it did not carry out any independent verification of schedules and held that no developing country Member had the resources required to examine in detail every other Member's Schedule, not only in connection with the Agreement on Agriculture, but also the other agreements. Brazil had relied on the good faith of all Members to complete their Schedules in accordance with their negotiated obligations.

4.137 The **Complainants** did not agree that the EC's Schedule contained a "scheduling error", that the error was shared, or excusable, as alleged by the European Communities (see paragraphs 4.124, 4.129, and 4.150). In any case, the European Communities' claim was undermined by the absence of any subsequent efforts by the European Communities to rectify this "error". In their view, the European Communities had committed more than a technical oversight, as it had failed to meet fundamental obligations in relation to its reduction commitments on a scheduled agricultural product under the Agreement on Agriculture. The Complainants sustained that the European Communities was itself responsible for the scheduled levels of bindings of base period and final commitment levels and that its schedule was developed in the full knowledge that these commitment levels were irrevocable. The European Communities knew that, unlike tariff bindings, there was no WTO procedure for the deconsolidation of scheduled bindings on export subsidy reduction commitments, and that it would be accountable under the terms of Article 10.3 of the Agreement on Agriculture in relation to Articles 3.3, 9.1 and 10.1, for any exports in excess of reduction commitment levels.

4.138 **Brazil** observed that it was not the first time that a WTO Member allegedly had erred in the preparation of its schedule and pointed to Hungary's case in 1996 which involved an error in establishing base period levels for export subsidy commitments. Brazil recalled that Hungary was not allowed to correct its error. However, Hungary obtained a waiver from the General Council allowing for a transitional period within which Hungary would bring its export subsidies into conformity with

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\(^{147}\) Exhibit COMP-8, p. 9.  
\(^{148}\) L/5113, para. 33.  
\(^{149}\) For example, Exhibits COMP-1, 2, 4, 10, 11, 12, 13, 17; and EC Regulation No. 1260/2001.  
\(^{150}\) Exhibit ALA-5.
its reduction commitments, as originally specified in its Schedule.\textsuperscript{151} Brazil also recalled the European Communities' standpoint in those circumstances.\textsuperscript{152}

4.139 The \textbf{Complainants} agreed with the European Communities (see paragraph 4.129) that Article 79 of the \textit{Vienna Convention} set out the process by which an error can be corrected in a treaty. However, the nature of the error addressed was clarified by Article 48.3 of the \textit{Vienna Convention} which stated that Article 79 applied to an "error relating only to the wording of the text of a treaty", i.e., addressing situations where there were drafting errors in the treaty text, and only applying in situations "where the parties are agreed that it contains an error". The Complainants asserted, therefore, that Article 79 had no application to the case of a contracting State failing to meet its obligations under a treaty. Article 48 of the \textit{Vienna Convention} dealt with the much more serious case of error that might be invoked by a State to invalidate its consent to be bound by a treaty. A State could not invoke an error to invalidate its consent to be bound by a treaty where the State had "contributed by its own conduct to the error or if the circumstances were such as to put that State on notice of a possible error". Further, a mistake as to (or ignorance of) the law did not constitute an error as to a fact or situation. In the present case, the requirements of Article 48 were thus not met, because, were there an error, the European Communities not only contributed to it, but made it. \textbf{Brazil} added that, under the \textit{DSU}, the Panel did not have the authority to permit the European Communities to correct a scheduling error. Moreover, \textbf{Thailand} underlined that under Article 48, a State may invoke error only where "the error relates to a fact or situation which was assumed by that State to exist at the time when the treaty was concluded…". The fact or situation that the European Communities assumed existed, in Thailand's understanding, was that no export subsidies were granted to C sugar, as it could not have anticipated the ruling in \textit{Canada – Dairy}. However, a mistake as to (or ignorance of) the law did not constitute an error as to a fact or situation.\textsuperscript{153}

4.140 The \textbf{Complainants} held that all Members were obliged to abide by Article 9.1(c) of the \textit{Agreement on Agriculture}, as interpreted by the Appellate Body. \textbf{Australia} recalled the statement it had made on adoption of the final Canada Dairy report by the DSB, supporting the compliance by all WTO Members of their export subsidy reduction commitments.\textsuperscript{154} Furthermore, Australia considered that the European Communities had not availed itself, as a matter of prudential practice, of the opportunity to undertake an assessment of the application of Article 9.1(c) to C sugar against the export subsidies identified in the Modalities Paper. \textbf{Brazil} pointed out that, regardless of whether it had taken the Appellate Body "no less than three successive rulings" (see paragraph 4.127) to define a precise test, the basic economic principle on which the \textit{Canada – Dairy's} allegedly "novel" and "unanticipated" interpretation by the Appellate Body had been presaged by both Jacob Viner in 1923, as well as by GATT Article XVI:1. According to Brazil, Viner had recognized\textsuperscript{155} that this "dumping" could take the form of "bounty dumping" financed by governments.

4.141 Referring to the European Communities' analysis in paragraph 4.128, the \textbf{Complainants} pointed out that the scope of the \textit{Agreement on Agriculture} (or the other WTO agreements) was not limited to measures adopted after its entry into force and that the WTO did not allow the "grandfathering" of past practices that were inconsistent with its provisions. Many measures that

\textsuperscript{151} WT/GC/M/23, p. 17.
\textsuperscript{152} The European Communities had taken the view that: "each Member had to respect its commitments, in particular since there were no procedures available which would allow such corrections. The European Communities were not convinced, on the basis of the evidence provided, that the situation was the result of an error and urged Hungary to comply with its commitments", G/AG/R/5, 5 July 1996, para. 13.
\textsuperscript{154} Exhibit EC-11, para. 18.
existed before the *WTO Agreement* came into effect – including, for example, the US foreign sales corporation tax rules challenged by the European Communities itself – had since been found to be inconsistent with one or more of the WTO agreements. The European Communities, therefore, could not argue that, because of its wrong judgement, it ought to be allowed to correct its Schedule. A Panel finding to the contrary would have troubling implications for future negotiations. **Thailand** added that there was thus no basis in law or logic that would permit the re-interpretation of an export reduction commitment in the light of jurisprudence that emerged after the commitment was made. Thailand suggested that this could possibly be done by the membership under the procedures for interpretations set out in Article IX:2 of the *Marrakesh Agreement Establishing the WTO (WTO Agreement)*, but certainly not by a panel in the framework of a proceeding under the **DSU**.

4.142 Thailand stressed that it would not be consistent with the principle of good faith if the European Communities were the only Member of the WTO that would effectively be exempted from this obligation through a re-interpretation of its export reduction commitments in the light of the allegedly unexpected consequences of the Appellate Body's interpretation of Article 9.1(c). Thailand considered that in invoking the principle of good faith, the European Communities was actually asking the Panel to replace the export subsidy reduction commitments that it assumed in its schedule, with the export subsidy reduction commitments that it claimed it would have assumed if it had known of the Appellate Body's interpretation of Article 9.1(c) at the time when it formulated its reduction commitments. Alternatively, the European Communities was asking the Panel to deny Thailand the right to invoke Article 9.1(c) in **DSU** proceedings because, allegedly, Thailand too, could not have expected that interpretation. WTO Members, including the European Communities, would be extremely concerned if panels were to begin dividing the Appellate Body's rulings into "expected" and "unexpected" rulings and were to refuse to give full effect to any "unexpected" rulings.

4.143 The **European Communities**, referring to the Complainants' assertions in paragraphs 4.130 and 4.133, reiterated the points made in paragraphs 4.123-4.124. Since the "base quantity" was part of the EC's Schedule and, therefore, part of the text of the *WTO Agreement*, the European Communities sustained that "an examination of the ordinary meaning of the terms of a treaty must take into account all of those terms"\(^\text{156}\), and in particular, the Modalities Paper, which, although not a covered agreement, and not explicitly mentioned in the *Agreement on Agriculture*, was not deprived of interpretative value. If exports of C Sugar were found to benefit from export subsidies, it would follow that the figures in the EC Schedule would be inaccurate as a matter of fact, because they would include only part of the total "quantity of subsidized exports", and the same would be true for the "base quantity". Therefore, the European Communities was not pleading that its consent to the *WTO Agreement* was invalid because it made an error with respect to facts outside the treaty, or with respect to the interpretation of the treaty. Rather, the European Communities' contention was that the Complainants' interpretation of Article 9.1(c) would have the necessary implication that there was an obvious error in the text itself of the treaty, due to a manifest discrepancy between the meaning of the headings in the EC's Schedule and the figures shown under those headings. In the European Communities' opinion, that discrepancy could not be ignored by the Panel and needed to be resolved by way of interpretation. The interpreter's task, in turn, was to reach an interpretation which gave meaning and reconciled all the terms of the treaty.

4.144 With respect to the Chairman's Note on the Modalities Paper, the European Communities contended that it meant that WTO Members could not bring claims under the **DSU** based on the violation of the Modalities Paper, but not that that text was irrelevant for the interpretation of the *Agreement on Agriculture*. The European Communities emphasized that the Modalities Paper was reached after protracted negotiations among participants, with a view to imposing specific obligations upon themselves, was drafted in mandatory terms, and purported to be binding, not mere "scheduling guidelines", such as those used for GATS Schedules. Despite its temporary nature, the Modalities

\(^{156}\) Appellate Body Report on *Korea – Various Measures on Beef*, para. 96.
Paper was an "agreement". It had, in fact, exhausted its legal effects upon the conclusion of the **WTO Agreement**, which, in the European Communities' view, explained why it had not been carried over to the **Agreement on Agriculture**. The European Communities also asserted that, in practice, the participants in the Uruguay Round had treated the Modalities Paper as a binding agreement, since the purpose of the "verification process" was to check the conformity of the schedules with the Modalities Paper. Citing Article 1(a) of the **Vienna Convention**, the European Communities held that the term "agreement" could encompass not only treaties but also informal and/or non-binding agreements. The Modalities Paper was thus "context", not "preparatory work". In accordance with the basic rule of interpretation of Article 31.1, treaty provisions must be interpreted always in their context, and, in the European Communities' view, this included also the elements falling within Article 31.2 (a).

4.145 However, in the alternative the European Communities submitted that, if the Panel were to conclude otherwise, it would still be justified to resort to the Modalities Paper under Article 32 of the **Vienna Convention** as preparatory work. It was precisely because the Modalities Paper was drafted with a view to agreeing on the commitments to be scheduled subsequently in the **WTO Agreement**, that it must be considered as made "in connection" with that Agreement. The European Communities stressed that the preamble of a treaty, which by definition imposed no legal obligations, was classified as "context" under Article 31.2 of the **Vienna Convention** (see also paragraph 4.149).

4.146 In relation to the argument presented in paragraph 4.138, the European Communities clarified that when Hungary had claimed an error, the European Communities had not taken the position that scheduling errors were irrelevant *per se*. Rather, the European Communities' position was that there had been no error. The European Communities also pointed out that Hungary, unlike the European Communities in this case, had not claimed in 1996 that the error had been shared by the other Members. The European Communities also explained that none of its claims involved the application of Article 48 as that provision, in its view, exclusively addressed the conditions under which error may be invoked in order to invalidate a State's consent to a treaty (see paragraph 4.139). It did not exhaust all the possible legal consequences of error. In the present dispute, the European Communities had not contended that its consent to the **WTO Agreement** was vitiated by error, but rather that the purpose of Article 48 was to allow the party that "made" an error to plead that such error invalidated its consent. If the State which "made" the error were precluded, for that reason alone, from invoking Article 48, that provision would become inapplicable. The issue, addressed by the exception in paragraph 2 of Article 48, was not who "made" the error, but rather whether the State that "made" the error and that pleaded the invalidity "brought the error upon itself".

4.147 The European Communities was not convinced by Brazil's arguments in paragraph 4.136 because of the substantial difference between the quantity mentioned in the schedule (1.617 million tonnes) and the total quantity of EC exports during the base period (4.788 million tonnes). Given Brazil's "compelling interest" in the sugar sector, the European Communities considered that the Brazilian authorities would have had the time to compare European Communities' draft schedule with the ISO or other easily available statistics, during the course of a three-year period. The European Communities noted that Brazil was the world's largest exporter of sugar and that the European Communities was the world's second largest exporter and the main provider of export subsidies for sugar. For geographical reasons, the European Communities was also Brazil's most direct competitor in most export markets. Further, the European Communities asserted that LMC data were available before 2000, and that subscriptions to the LMC reports was already possible. In any case, it was totally irrelevant whether or not the Complainants were aware in 1994 that the exports of C sugar were made below total cost of production because at that time nobody thought that this could be of any relevance whatsoever for establishing the existence of a "payment". The Complainants' position summarized in paragraphs 4.140-4.141 presupposed that, in 1994, they had anticipated the interpretation of Article 9.1(c) made by the Appellate Body in **Canada – Dairy**.
4.148 Responding to the European Communities' argument in paragraph 4.144, Thailand pointed out that the Modalities Paper was analogous to the GATS scheduling guidelines, which "were to assist in the preparation of … national schedules of initial commitments." From Thailand's perspective, there was consequently no reason to give the GATS scheduling guidelines an interpretative value under the Vienna Convention different from that of the Modalities Paper. Thailand noted that the interpretative value of the GATS guidelines in the Mexico-Telecommunications case was limited to that of a supplementary means of interpretation under Article 32 of the Vienna Convention. Furthermore, the Modalities Paper was established only by those Members of the WTO who participated in the Uruguay Round and Article 31.2(a) of the Vienna Convention would apply to these arrangements only if they were made by "all" Members of the WTO, including those who acceded to the WTO at a later stage. The Modalities Paper thus could not be seen to be accepted by all parties as it was not formally part of the Agreement on Agriculture, nor part of the package of obligations "accepted" by acceding Members. Thailand also pointed to the instances when the European Communities had expressed contrary views on this issue.

4.149 Referring to the Complainants arguments in paragraph 4.148 and to the panel's findings in EC – Tariff Preferences, the European Communities asserted that subsequent accession to a treaty involved an implicit acceptance of all relevant contextual elements for the interpretation of that treaty. The panel had even concluded that an informally adopted UNCTAD document, established by a special negotiating group, was "context" within the meaning of Article 31.2(a), even though that document expressly stipulated that it was not legally binding. The European Communities found illogical that an agreement which was "context" when the treaty was concluded ceased to be so subsequently. What mattered was whether all the parties that concluded the treaty were parties of the agreement made in connection with the conclusion of that treaty.

(b) Good faith and estoppel

4.150 If, despite the arguments by the European Communities summarized in Sections IV.D.1, IV.D.2 and IV.D.3(a) above, the Panel were to conclude that exports of C sugar were in excess of the European Communities' reduction commitments, the European Communities submitted, subsidiarily, that by claiming that the European Communities was in breach of those commitments, the Complainants were not exercising reasonably their rights under the DSU. The European Communities held that the Complainants were seeking to benefit from an excusable scheduling error, which would unfairly advantage the Complainants, and upset the balance of concessions. Furthermore the Complainants were estopped from bringing this claim because they had contributed to that error through their own conduct. For those reasons, the European Communities considered that the Complainants were acting inconsistently with the general principle of good faith and with their obligation under Article 3.10 of the DSU to engage in dispute settlement procedures in good faith.

4.151 In addition to the arguments and definitions already summarized in paragraph 4.122, the European Communities submitted that the principle of good faith was "at once a general principle of law and a principle of general international law" that "informs" all covered agreements. The European Communities cited jurisprudence in support of the view that there was a basis for a dispute.

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157 Scheduling of Initial Commitments in Trade in Services: Explanatory Note MTN.GNS/W/164 (3 September 1993), para. 1.
settlement panel to determine, in appropriate cases, whether a Member had not acted in good faith, and that the principle of good faith controlled not only the performance of obligations but also the exercise of Members' rights, enjoining them to exercise their WTO rights "reasonably" and prohibiting the "abusive" exercise of those rights. The European Communities described the principle of good faith as "pervasive" in certain cases, particularly "if post-determination evidence relating to pre-determination facts were to emerge, revealing that a determination was based on ... a critical factual error." The European Communities also held that the exercise of the right to submit claims to a panel had to be used reasonably, and in accordance with Article 3.10 of the DSU and with the general principle of good faith.

4.152 The European Communities also referred to estoppel as a general principle of international law, which followed from the broader principle of good faith. The European Communities argued that it was one of the principles which Members were bound to observe when engaging in dispute settlement procedures, in accordance with Article 3.10 of the DSU. The European Communities referred to several descriptions of the operation of the principle of estoppel as a basis for its claims and argumentation, and held that the following features were generally accepted as essential elements of estoppel: the party invoking estoppel must have been induced to undertake legally relevant action or abstain from it; by relying in good faith upon clear and unambiguous representations by the other State; and reliance must prejudice the addressee, i.e., subsequent deviation from the original representation must cause damage to the relying State, or result in advantages for the representing State. Estoppel might arise not only from express statements, the European Communities continued, but also from various forms of conduct, including silence, where, upon a reasonable construction, such conduct implied the recognition of a certain factual or juridical situation.

4.153 In view of the above, the European Communities concluded that, if the Complainants held that they were already of the view, at the time of the conclusion of the WTO Agreement, that exports of C sugar benefited from export subsidies, the European Communities considered that they would not have acted in good faith because they had failed to advise the European Communities to include those exports in the base quantity. If, on the other hand, the Complainants confirmed that they believed until recently that exports of C sugar did not involve export subsidies, the European Communities submitted that they would not be acting in good faith by seeking to take advantage of an excusable and common scheduling error in order to exact from the European Communities a concession that was never negotiated with, or requested from, the European Communities during the

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165 The European Communities gave the following examples of judicial application of the principle of estoppel in support of its view: Arbitral Award by the King of Spain Case (ICJ Reports, 1960, 192 at 213); Temple of Preah Vihear Case (ICJ Reports, 1962, 6 at 32); opinions of Judges Alfaro and Fitzmaurice in the Temple of Preah Vihear Case (ICJ Reports, 1962, 39-51, and 61-51); Brownlie, Principles of Public International Law (Oxford, 2003), p. 616); J.P. Müller and T. Cottier, in Encyclopaedia of Public International Law, Ed. Max Planck Institut, North Holland, 1992, p. 118.
166 According to the European Communities, the panel in India – Autos suggested that the principle of estoppel was applicable in WTO disputes (footnote 364). The panel in Argentina – Poultry Anti-Dumping Duties declined to rule on this issue, in view of the fact that the conditions identified by Argentina for the application of that principle were not present (footnote 58). The European Communities further stated that a number of other panels have addressed and rejected estoppel arguments, having regard to the specific facts of the dispute, without questioning the applicability of this principle to GATT/WTO disputes. See Panel Report on EEC (Member States) – Bananas I, para. 362; Panel Report on Guatemala – Cement II, paras. 8.23-8.24, and Panel Report on EC – Asbestos, para. 8.60.
167 The European Communities referred in this regard to the judgement of the ICJ in the Temple of Preah Vihear Case (ICJ Reports, 1962, 6-32 32); see also opinions, in the same case, of: Judge Fitzmaurice, p. 62; Judge Alfaro, pp. 41-42; case law summarized by Judge Alfaro at pp. 43-51 of his opinion.
Uruguay Round, and for which no compensation was paid nor received. Referring to its arguments concerning the awareness, lack of reaction, and shared understanding in paragraphs 4.124 and 4.126, the European Communities submitted that it legitimately should have been able to rely upon the Complainants' conduct when it decided not to include exports of C sugar in the base levels. Its position had therefore been prejudiced as outlined in paragraph 4.129. To the extent that the alleged violation resulted from the non-inclusion of the exports of C sugar in the scheduled base levels, the Complainants were thus estopped from claiming that the European Communities was in breach of its reduction commitments.

4.154 The Complainants rejected the European Communities' arguments that they had sought to exercise their rights unreasonably, that panels had the power to determine whether a Member had not acted in good faith, and that Article 3.10 imposed a requirement on Members' rights to submit claims to a panel. Further they rejected the European Communities' argument that their conduct had given rise to an estoppel.

4.155 Australia submitted that the jurisprudence cited by the European Communities in support of its argument summarized in paragraph 4.151 could not be relied upon, because of selective or partial quotation of the relevant sections. The Appellate Body had considered that the fact that a Member had violated its obligation, in and of itself, did not lead to a finding that the Member had not acted in good faith. 168 The doctrine of "abuse of right" cited by the European Communities had been referred to in the context of Article XX of GATT 1994, the operation of which involved a balance between the rights of Members when an exception was invoked. 169 That balance would be upset if a Member were permitted to "abuse or misuse its right to invoke an exception". In the present case, the Complainants were not seeking to rely on an exception which needed to be balanced against the treaty rights of other Members to ensure those rights were not devalued. Rather, the Complainants were seeking to exercise their rights to engage in dispute settlement in relation to the breach by another Member of its obligations under the WTO agreements. Finally, in another instance, the Appellate Body had expressly declined to express a view on the matter. 170

4.156 With respect to the European Communities' arguments in paragraphs 4.150-4.152, the Complainants responded that Article 3.10 dealt with the good faith observance of procedural rules 171 and did not apply to the right of a WTO Member to bring a particular claim. As such, it could not provide the basis for a claim of estoppel. Moreover, Article 3.10 did not expressly refer to a principle of estoppel. Since WTO Members had a fundamental right to pursue dispute settlement proceedings they could not be estopped from exercising that right. The Complainants considered that, although the principle of estoppel was linked to the general principle of good faith 172, this did not mean that a WTO Member could rely on that principle to defeat a claim brought by another Member. The principle of estoppel was not imported into the WTO agreements by the reference in Article 3.2 of the DSU to the customary rules of interpretation of public international law, and it was not a customary rule of interpretation.

4.157 The Complainants contended that the reference to good faith in Article 3.10 applied only "if a dispute arises" and therefore was relevant not to the decision to pursue dispute settlement, but to how the parties "engage in these procedures" after the "dispute arises". Article 3.10 of the DSU could not provide the basis for a claim of estoppel. They further contended that the European Communities ignored the distinction between Article 3.7 of the DSU, which regulated the initiation of a dispute ("before bringing a case"), and Article 3.10 of the DSU, which regulated the conduct of Members

169 Appellate Body Report on US – Shrimp, para. 158
172 1984 ICJ Reports, p. 305, para. 130.
engaged in dispute settlement procedures ("if a dispute arises"). The European Communities' argument that the Complainants were barred from bringing complaints as they were not acting in good faith, or were estopped from doing so, related to their obligations under Article 3.7 of the DSU, as it was that provision which addressed the launching of cases by Members, by providing in part that "[b]efore bringing a case, a Member shall exercise its judgement as to whether action under these procedures would be fruitful". According to the Complainants, the weight to be given under Article 3.7 to the judgement of a Member bringing a case was emphasized by the Appellate Body in EC – Bananas III, where it found that "a Member has broad discretion in deciding whether to bring a case against another Member under the DSU. The language of ... Article 3.7 of the DSU suggests, furthermore, that a Member is expected to be largely self-regulating in deciding whether any such action would be "fruitful". Also, the Appellate Body had confirmed that complainants were entitled to benefit from the presumption of good faith performance of the obligations under Article 3.7 of the DSU as: "given the "largely self-regulating" nature of the requirement in the first sentence of Article 3.7, panels and the Appellate Body must presume, whenever a Member submits a request for establishment of a panel, that such Member does so in good faith, having duly exercised its judgement as to whether recourse to that panel would be "fruitful". Article 3.7 neither requires nor authorizes a panel to look behind that Member's decision and to question its exercise of judgement. Therefore, the Panel was not obliged to consider this issue on its own motion."

4.158 The Complainants asserted that, although the principle of estoppel had been raised by parties in earlier disputes, it had never been applied by a panel in determining a claim before it. Australia noted that the EC argumentation seemed to imply that a number of panels did not question the applicability of estoppel in disputes. Referring in particular to India – Autos, Australia contended that the panel did not suggest that estoppel "was applicable in WTO disputes", but commented, in footnote 364 to its report, that "there may be an argument that a general principle such as estoppel may apply to WTO dispute settlement". Australia questioned whether the cited statement expressed support for the application of estoppel in the WTO. Brazil noted that the European Communities had not pointed to one single instance in which a panel had relied on the estoppel doctrine to deny a WTO Member access to dispute settlement procedures to resolve a substantive dispute or to reject an individual claim ab initio. Brazil also recalled the standpoint the European Communities had adopted in past disputes, when it had maintained that a WTO Member's decision to pursue dispute settlement proceedings was not subject to a rule of good faith; that Members had a "fundamental right to resort to dispute resolution at any time; and that such right could be restricted only by clear and unambiguous language."

4.159 The Complainants further asserted that the conditions for the application of estoppel were not present in these proceedings, and that the European Communities had not presented the facts necessary to justify the invocation of the doctrines of estoppel or good faith in this dispute. Australia submitted that if, despite its arguments to the contrary, the Panel were to find that the principle of estoppel could be applied in WTO disputes, and accepting arguendo the content of the principle put forward by the European Communities, its conduct could in no way give rise to estoppel. This content included: a "clear and unambiguous representation" by the Complainants, and that the European Communities was "induced" to act in reliance of that representation. In the Complainants'
view, these conditions were without a doubt not satisfied in this case. First, the European Communities had not argued that it relied upon "clear and unambiguous representations" made by the Complainants, but rather that it relied upon their "silence" (see for instance paragraph 4.152). The Complainants recalled that, in EEC (Member States) – Bananas I, the panel had rejected a similar argument presented by the European Communities, noting that: "estoppel could only result from the express, or in exceptional cases implied, consent of such parties or of the contracting parties". Applying this standard the panel had found that "[t]he mere inaction of the contracting parties could not in good faith be interpreted as an expression of their consent to release the EEC from its obligations under Part II of the GATT". 179

4.160 Since silence could only amount to representation in "exceptional circumstances" such as where there was a duty or obligation to object, Thailand noted that the European Communities had pointed to no legal authority, as there was none in its view, to support a lower threshold of "reasonable expectations to speak". Moreover, the Complainants were under no "duty to object" 180 during the bilateral meetings or the verification process and furthermore could not reasonably be expected to do so. In this respect, Thailand recalled that the purpose of the verification process, referred to by the European Communities in these proceedings as giving an opportunity to the Complainants to object (see paragraph 4.126), was to give each participant in the Uruguay Round the opportunity to verify whether the export subsidy reduction commitments assumed by the other participants were consistent with the guidelines for negotiations set out in the Modalities Paper. The purpose of the verification process was not, in Thailand's view, to alert participants to instances in which they had not retained options open to them under the Modalities Paper or to settle disputes about the consistency of the commitments assumed with the Agreement on Agriculture. Therefore, the Complainants' silence could not be deemed to have constituted an implicit agreement, seemingly because they failed to object during the verification process.

4.161 Transposing the reasoning of the Appellate Body in EC – Computer Equipment 181, Thailand also contended that the Complainants only had the duty to ensure that their export interests were safeguarded. Thailand had not therefore "acted in bad faith by not advising the EC" to include C sugar exports in the base period levels. It was for the European Communities to define its export subsidy reduction commitments in terms which suited its needs. The European Communities could not, for these reasons, legitimately expect that other WTO Members advise it to raise its base period levels so that it could grant more export subsidies. There were many reasons why a participant in a multilateral trade negotiation might not wish to maintain measures affording protection to domestic producers even though such measures were specifically provided for by the negotiating modalities. Many participants had used such negotiations as a means to overcome domestic interests opposed to trade liberalization or had simply agreed to liberalize beyond the agreed modalities in an effort to advance their national economic interests. Furthermore, even if its silence were held to constitute a representation, the European Communities would need to demonstrate that it in fact relied on Thailand's silence, and its own decision not to assume export subsidy reduction commitments for sugar, when determining the scope of the European Communities' own export subsidy commitments for sugar. 182 Yet, in Thailand's knowledge, there was no record to suggest that the European Communities had relied on the Complainants' silence when the European Communities scheduled its base quantity levels and that it would have acted differently if the Complainants had raised objections. Thailand therefore did not believe that the assumption that the European Communities would have increased the base period levels if advised of its "scheduling error", and that the Complainants were aware of this, could be advanced.

179 GATT Panel Report on EEC (Member States) – Bananas I, paras. 361 and 363.
180 See Temple of Preah Vihear Case (ICJ Reports, 1962) p. 62; see also Panel Report on Guatemala – Cement II, footnote 791 ("it is clear that not any silence can be considered to constitute consent").
4.162 The Complainants contested the premises upon which the European Communities had based its argumentation on estoppel. Recalling the situation with regard to the availability and access to the relevant sources of information during the Uruguay Round (see paragraph 4.135), Australia contended that the European Communities provided substantial manufacturing and export subsidies to sugar processors but did not consider it appropriate to conduct a survey of the EC sugar companies to establish how their loss-making activities were being financed. Consequently, any expectation by the European Communities that Australia was in a position to speak, or had a “duty to speak”, was not reasonable. Furthermore, as this dispute involved claims that the European Communities was not complying with its WTO treaty obligations, it was the European Communities' performance of its treaty obligations that was at issue. In particular, those treaty obligations which could allegedly be extinguished by the European Communities' assertion that, prior to the conclusion of the WTO treaty, the Complainants had a responsibility to draw certain matters to its attention.

4.163 In Brazil’s view, the implications of the European Communities' argumentation were that any WTO Members that were initiating dispute settlement proceedings regarding measures in effect before the WTO agreements entered into force were acting in bad faith, in that they should be treated as having accepted the measure by their “silence” both before and since the WTO agreements entered into force. This suggested that WTO Members could initiate dispute settlement proceedings against the European Communities only when the European Communities itself knew during the Uruguay Round that its measures would be inconsistent with the WTO agreements.

4.164 Thailand also argued that the obligations of a WTO Member were obligations towards all other WTO Members. A Member of the WTO invoking estoppel would therefore have to establish that it was induced to act in reliance of the representations of all the other WTO Members. If not, the doctrine of estoppel would lead to a complex and incongruous web of the rights and obligations among WTO Members inconsistent with the multilateral character of WTO law. For instance, the rights and obligations of Members that acceded to the WTO and those of the original Members of the WTO might differ. It was therefore not surprising that no panel to date had applied the principle of estoppel in the GATT or WTO context.

4.165 The European Communities replied that the rights and obligations under the DSU were expressly provided in Article 3.10 of the DSU as clarified by the Appellate Body in US – FSC, and were, inter alia, that Members must exercise their right to institute dispute settlement proceedings "in good faith". The general principle of good faith and Article 3.10 of the DSU imposed additional requirements upon Members to prevent them, in particular, from exercising their right to request a panel in an abusive manner so as to exact a manifestly unfair advantage, or in circumstances where a Member was estopped from doing so by virtue of its previous conduct. The suggestion that the exercise of this right should be subject exclusively to Article 3.7 of the DSU found no support in the language of Article 3.10, which, according to the European Communities, covered any action regulated by the DSU, including that taken by Members under Article 6 of the DSU. The European Communities recognized however that Article 3.7 of the DSU was an expression of the principle of good faith. But that provision did not exhaust all the requirements imposed by that principle with respect to the initiation of dispute settlement proceedings because it exclusively concerned the issue of whether such action would be "fruitful", i.e. the necessity or opportunity of bringing a case, with a view to prevent frivolous complaints. According to the European Communities, this argument found support in the Appellate Body statement in US – Corrosion-Resistant Steel Sunset Review. 183

4.166 With respect to the Complainants' analysis in paragraph 4.158, the European Communities considered that a "dispute "arises" from the moment that two Members disagreed on the interpretation of the WTO Agreement, whether or not they had taken any formal action under the DSU, as evident in Article 4.7 of the DSU. The term "dispute settlement procedures" used in Article 3.10 comprised all

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183 Appellate Body Report on US – Corrosion-Resistant Steel Sunset Review, para. 86.
the "procedures" regulated by the DSU and not just the panel phase, including, inter alia, the provisions of Article 6. It was also incorrect that the exercise of the right to request a panel was subject exclusively to Article 3.7 of the DSU. That provision was but one of the expressions of the principle of good faith.\textsuperscript{184}

4.167 Responding to the argument summarized in paragraph 4.164, the European Communities considered that the principle of estoppel did not operate by derogating or amending tacitly the treaty rights and obligations of the parties concerned but was a procedural defence which precluded one party from exercising a right vis-à-vis another party but without modifying the substantive obligations of that party.\textsuperscript{185} In the present case, the European Communities' contention was that the Complainants were precluded from bringing a claim under Article 9.1(c) and therefore that the Panel should reject their claims, even if it upheld them in substance. Since estoppel did not alter the substantive rights of Members under the \textit{WTO Agreement} but only the exercise of those rights, the European Communities was of the view that it could operate exclusively between two Members.

4.168 Further, the European Communities underlined that estoppel was a matter of adjectival, rather than substantive, law and accordingly the effect of a true estoppel was confined to the parties.\textsuperscript{186} The contention that estoppel amounted to "consent" (see paragraph 4.160) was wrong and without foundation in public international law. Referring to recent panels' interpretation of that notion\textsuperscript{187}, the European Communities sustained that the existence of estoppel must be established from the perspective of the party who claimed it. The issue was whether that party could rely legitimately on the representations made by the other party, regardless of whether such representations amounted to "consent", as in, for example, circumstances where representations made by error or inadvertence could be legitimately relied upon and give rise to estoppel. The European Communities considered that assimilating estoppel to "consent" would render largely superfluous the institution of estoppel. In the European Communities' view, if a party "consented" to something, it gave up its substantive rights, and there was no need for the other party to invoke a procedural defence, such as estoppel, against the exercise of such rights.

4.169 The European Communities submitted that from the fact that the Complainants were aware that exports of C sugar were not included in the base quantity, and from the fact that they did not raise any question, it could reasonably infer that the Complainants shared, at the time of the conclusion of the WTO Agreement, its view that exports of C sugar did not benefit from export subsidies. In this regard, the European Communities also considered that silence could be legitimately construed as a representation of lack of objections, not only where there was a "duty to speak", but also in circumstances where it was reasonable to expect that the other parties would speak. The European Communities asserted that the existence of estoppel required that the party relying on the representations made by the other party suffered a "prejudice" as a result of such reliance. In the present case, the European Communities sustained that upholding the Complainants' allegations would unfairly penalize the European Communities, as outlined in paragraph 4.129, for an unanticipated and until recently, shared, scheduling error. This would upset the balance of concessions.

4.170 As further proof of the existence of a shared understanding among WTO Members, the European Communities recalled its reasoning in paragraph 4.69. The fact that, for example, Brazil or Thailand, considered that their measures, and therefore also the European Communities’ measures, did not provide export subsidies, amounted to a "clear representation" in the European Communities'
view. Additionally, the Complainants’ lack of reaction during the Uruguay Round clearly indicated to
the European Communities that they shared the understanding that the C sugar regime did not provide
export subsidies.

4.171 The Complainants responded that the sugar policies applied by other WTO Members
referred to by the European Communities were irrelevant in these Panel proceedings.

4.172 Thailand, in turn, submitted that it was precisely because the doctrine of estoppel was a
procedural defence precluding a party from exercising its rights vis-à-vis another party, that it would
create discrepancies between the rights that different WTO Members might assert under the DSU.
The European Communities’ argumentation implied that in future multilateral trade negotiations
Members would be forced to make objections against another Member’s attempts to qualify
obligations under WTO law through notes in schedules, lest they would risk losing their rights under
the WTO. This would create an onerous negotiating environment, where the better resourced WTO
Members would have an advantage over the smaller and poorer countries. WTO law would not
provide an efficient, secure and fair framework for multilateral trade negotiations if WTO Members
were allowed to use the silence of other Members during the negotiations as an excuse for not
performing their commitments.

E. ACP/INDIA “EQUIVALENT” SUGAR

4.173 The Complainants claimed that the European Communities had exceeded its export subsidy
reduction commitments, inter alia, by according export subsidies to ACP/India equivalent sugar. They
recalled that the European Communities had the burden of proof under Article 10.3 of the Agreement on
Agriculture to establish that it had not exceeded its export subsidy reduction commitments.

4.174 The Complainants asserted that they were not questioning the preferential access of
ACP/India sugar to the EC market and were not asking for a change in the requirement that
ACP/India sugar be purchased at intervention prices. Rather, the Complainants were seeking to
address the measures which, in their view, did not conform to the WTO disciplines, notably by asking
the European Communities to cease exporting sugar in excess of its reduction commitments.

1. Article 9.1(a) of the Agreement on Agriculture

4.175 The Complainants submitted that the European Communities granted export subsidies listed
in Article 9.1(a) of the Agreement on Agriculture to exports of ACP/India equivalent sugar. By virtue
of Article 2 of the Agreement on Agriculture, the European Communities' budgetary outlay and export
quantity reduction commitments covered this category of sugar notwithstanding the footnote inserted
in the European Communities' Schedule of Concessions. Consequently the European Communities
acted inconsistently with its obligations under Articles 3.3 and 8 of the Agreement on Agriculture.

4.176 The Complainants further submitted that a quantity of sugar that the European Communities
considered to be "equivalent" to the amount of sugar imported under preferential trade arrangements
was exported from the European Communities to third countries using export refunds. The export
refunds granted to ACP/India equivalent sugar were the same as the export refunds granted to A and
B quota sugar and thus these payments clearly constituted "direct subsidies" provided by government,
to firms, to the exporting industry and to producers of sugar, "an agricultural product", and were
"contingent on export performance", within the meaning of Article 9.1(a) of the Agreement on

188 The Complainants explained that, by bringing this case, they were not seeking to affect the
preferential access of the ACP countries and India to the EC market and were not requesting that the European
Communities withdraw the preferential market access it granted to those countries.
Agriculture. As the export refund system was identical to the system of export refunds for quota sugar, which the European Communities recognized to be covered by its export subsidy reduction commitments[^189], Article 9.1(a) brought within its scope such subsidies, which had to be, accordingly, subject to reduction commitments.

4.177 The Complainants pointed out that, as the European Communities had exported 1,725,100 tonnes of this sugar category alone during marketing year 2001-2002, such subsidized exports were in excess of the European Communities' scheduled commitment levels for that year[^190]. The Complainants submitted statistical data which suggested that most of the "preferential" sugar imported by the European Communities (principally into the UK) was actually consumed in the European Communities[^191]. The European Communities had also admitted that the export subsidies on "preferential" sugar were subsidies on EC quota sugar, up to a quantity limit of 1.6 million tonnes[^192].

4.178 The European Communities responded that the Complainants had failed to properly interpret the European Communities' scheduled commitments. The allegations that the European Communities had exceeded its export subsidy commitments should therefore be rejected. The European Communities explained that it had provided export refunds to an amount of exports equivalent to the sugar it imported under preferential import arrangements and that such exports were eligible to receive export refunds. The European Communities noted that its export statistics did not distinguish between refined sugar obtained from ACP/India equivalent sugar and other sugar.

4.179 According to the Complainants, the figures supplied by the European Communities in its submissions to the Panel, as well as its notifications to the Committee on Agriculture clearly indicated that it had exceeded its quantity commitment levels in marketing year 2001-2002[^193]. These figures constituted an admission on the part of the European Communities that, in that marketing year, it had granted export refunds to 2,651,900 tonnes of sugar amounting to €1,217,247,000. The Complainants also took note of the European Communities' categorization of quantity of sugar that benefited from these refunds into "ACP/India equivalent sugar" and "notified A+B sugar"[^194]. The European Communities had also confirmed that it was applying export subsidies to ACP/India equivalent sugar within the meaning of Article 9.1(a) of the Agreement on Agriculture, in line with the historical record[^171]. The Complainants recalled that, if the European Communities claimed that the exports of ACP/India equivalent sugar were not subsidized, it had the burden of proof, under Article 10.3 of the Agreement on Agriculture, to establish that no export subsidies applied to such exports.

4.180 The Complainants reiterated that their claim was based on the following premises: the export refunds were export subsidies within the meaning of Article 9.1(a) of the Agreement on Agriculture[^195]; the export refunds granted to ACP/India equivalent sugar and "notified A+B sugar" should be counted against the European Communities' reduction commitments; and, for marketing year 2001-2002, the European Communities' quantity commitment level was 1.273 million tonnes and budgetary outlay commitment level was €499.1 million. In their view, the European Communities' reduction commitments covered the exports of ACP and India equivalent sugar, given the European Communities' own admission that all the export refunds granted to sugar were export subsidies, and

[^189]: The European Communities notified certain export refunds for quota sugar. These refunds, provided under Article 27 of the Regulation, were the same as those provided to ACP/India equivalent sugar.

[^190]: Exhibit COMP-15, p. 17.

[^191]: The United Kingdom was the major importer of "Preferential" sugar (approximately 1.1 million tonnes), but exported less than 400,000 tonnes (104,000 tonnes to other EC member States and 383,000 tonnes to third countries). Source http://statistics.defra.gov.uk.

[^192]: EC advice at consultations 21/22 November 2002, confirming that the exports in question of 'Preferential sugar' were sourced from A and B quota. See also Exhibit COMP-11, p. 9; and L/4833 para. 2.19 (GATT Panel Report on European Communities – Refunds on Exports of Sugar).

[^193]: See Tables 10, 11, and 12 of the European Communities' first written submission.

[^194]: Exhibit ALA-6.
that the export refunds granted to all categories of sugar were subject to reduction commitments. The European Communities’ contention that its export subsidy commitment levels were significantly higher than the level cited by the Complainants found no basis in the EC’s Schedule, when considering the figures under the headings "annual and final outlay commitment levels" and "annual and final quantity commitment levels".

2. Exemptions through unilateral insertions in Schedules

4.181 Referring to the European Communities’ assertion before the WTO Committee on Agriculture that it had not assumed reduction commitments in respect of ACP/India equivalent sugar, the Complainants considered that such a position was legally untenable. They submitted that Members could not exempt themselves from their obligations under the Agreement on Agriculture by including reservations in their Schedule of Concessions that must be subsequently accorded the same, or greater weight, than any provision of a WTO Agreement with which the schedule text might directly conflict. To the extent that the European Communities purported to diminish its obligations under the Agreement on Agriculture, the footnote, in their view, constituted an impermissible reservation under international law.

4.182 The Complainants considered that, if Members could validly modify their obligations under the Agreement on Agriculture through entries in their Schedule, the purpose of Article XVI:5 of the WTO Agreement would be frustrated. The WTO Agreement foreclosed the possibility of making any reservation to the obligations under these Agreements. If Members were permitted to qualify their obligations under the Agreement on Agriculture or Article II of GATT through notes to their Schedules, the WTO Agreement would effectively be reopened by interpretation. The Complainants sustained that the Agreement on Agriculture did not provide for reservations of any kind, and in this respect, was different from GATS, which expressly permitted Members to impose "conditions and qualifications" on certain types of scheduled obligations. This principle was reinforced by Article 3.1 of the Agreement on Agriculture.

4.183 With respect to the Agreement on Agriculture, the Complainants submitted that a Member could not grant export subsidies without a corresponding reduction commitment. First, Article 3.1 made clear that export subsidy commitments expressed in a Schedule "constitute commitments limiting subsidization and are hereby made an integral part of GATT 1994." A Member may not use a footnote to negate "an integral part of GATT 1994."

4.184 The Complainants submitted further that Article 3.3 prohibited Members from providing export subsidies in respect of agricultural products specified in their Schedules "in excess of the budgetary outlay and quantity commitment levels specified therein". Further, Members "shall not provide such subsidies in respect of any agricultural product not specified in that Section of its Schedule". Thus, any subsidy provided to a scheduled agricultural product, such as sugar, was subject to the reduction commitments "specified" in a Member’s Schedule. In the Complainants’ view, export subsidies granted to an agricultural product were therefore either subject to reduction commitments in accordance with Article 9.2(b)(iv), or they were inconsistent with the requirements of the Agreement on Agriculture. There was no alternative category. The Complainants reasoned that, as sugar was a product "specified" in the EC’s Schedule, the European Communities was under the obligation to reduce its budgetary outlays and export quantities of subsidized sugar in accordance with its obligations.

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195 Exhibit COMP-21: The European Communities had replied that: "As indicated in footnote 1 of the table on export subsidies contained in Part IV, Section II of Schedule CXL, the EC is not undertaking any reduction commitment on exports of ACP or Indian sugar. Consequently, any financial assistance is not reported to the WTO. For information, these exports amount to approximately 1.6 million tonnes per year."

196 General Agreement on Trade in Services, Annex 1B to the Marrakesh Agreement Establishing the WTO, Articles XVII and XX.
scheduled commitments. In this context, the Complainants asserted that the reduction commitments under the first clause of Article 3.3 represented narrower commitments than the export subsidy commitments on unscheduled products mandated by the second clause of Article 3.3. 197

4.185 Having recalled the substance of Article 3.3, the Complainants held that, under Article 8, each WTO Member undertook not to provide export subsidies otherwise than in conformity with the Agreement on Agriculture and with the "commitments as specified" in the Member’s Schedule. The Complainants submitted that the footnote was not a "commitment" "specified" "in" a schedule because it did not provide "specific binding commitments" regarding "export competition". Article 8 specifically stated that all export subsidies must be "in conformity with this Agreement and with the commitments" set out in the Schedule of Concessions. By adding the conjunctive "and", the drafters left no doubt that it was not sufficient for a Member to act consistently with its reduction commitments; it must also act consistently with the Agreement on Agriculture and that Agreement permitted only those export subsidies that the Member agreed to reduce to specified levels. Further, neither Article 3, nor Article 8, could be given a meaning which was contrary to the letter and the spirit of those provisions. The Complainants emphasized that the provision of "specific binding commitments" regarding "export competition" was one of the objects and purposes of the Agreement on Agriculture, as reflected in its Preamble. The footnote therefore conflicted with both provisions.

4.186 Article 9.1 of the Agreement on Agriculture confirmed that Members were not entitled to select unilaterally the export subsidies in respect of which they made reduction commitments. In the chapeau of Article 9.1, the words "are subject to reduction commitments" left no choice to WTO Members, requiring that all export subsidies listed be subject to reduction commitments. The Complainants reasoned that, as long as an export subsidy fell within the terms of any of the subparagraphs of Article 9.1, it was subject to reduction commitments.

4.187 Lastly, Article 10.1 of the Agreement on Agriculture obliged Members to refrain from applying export subsidies not listed in Article 9.1 in a manner which circumvented their export subsidy commitments. In the Complainants' view, that provision also expressed the intent to confine the right of a Member to accord subsidies, to the subsidies that it was committed to reducing. Consequently, a footnote to a Schedule could not be used to create a category of scheduled agricultural products that were not subject to a Member's reduction commitments. The European Communities had therefore an unqualified obligation to subject those direct export subsidies to its reduction commitments, and the footnote could not override or invalidate the treaty text.

4.188 The Complainants submitted that GATT and WTO jurisprudence endorsed by the Appellate Body established that WTO Members could incorporate in their Schedule of Concessions only acts yielding rights, not acts diminishing obligations. The GATT and the Agreement on Agriculture did not permit reservations. In EC – Bananas III, the Appellate Body found that the ordinary meaning of the term "concessions" suggested that a Member may yield rights and grant benefits, but it cannot diminish its obligations, a principle further confirmed in EC – Poultry, and reaffirmed in Chile – Price Band System.

4.189 Any exception to the European Communities' commitments under the Agreement on Agriculture, in their view, would have had to be provided through a formal WTO waiver, in accordance with the provisions of Article IX:3 of the WTO Agreement. They noted that a waiver could only be granted in exceptional circumstances. The European Communities would also have needed to seek a waiver for any recalculation of base level outlays and quantities, given that it had

bound the base levels in its Schedule. The Complainants noted that the European Communities had neither sought nor received a waiver for the exclusion of ACP/India equivalent sugar from its WTO commitments.

4.190 The European Communities responded that a waiver was only necessary if the underlying situation was inconsistent with a Member's obligation. The European Communities pointed out that, while a waiver may be obtained with the support of only three quarters of the membership of the WTO, inserting a footnote into a Member's schedule required the agreement of all WTO Members.\textsuperscript{201}

In this context, the European Communities considered that, by virtue of Article 16 of the Vienna Convention, the Complainants had consented to be bound by the terms of the treaty footnote contained in the EC's Schedule, by ratifying the WTO Agreement. Thus, they had agreed to it. Denying any legal effect to the footnote would amount to finding that part of the WTO Agreement was inconsistent with another part of that Agreement, ultimately undermining the balance of concessions. According to the European Communities, this would also be contrary to Article 3.2 of the DSU which stated that dispute settlement "cannot add to or diminish the rights and obligations provided in the covered agreements."

4.191 The European Communities contended that schedules were an integral part of the WTO Agreement by virtue of Article 3.1 of the Agreement on Agriculture, and were therefore subject to the rules of interpretation of the Vienna Convention. The European Communities' export subsidy commitments were articulated in two components. The first component served to set the limits which were subject to reduction, while the second component (the footnote) set a fixed ceiling. The European Communities contended that, overall, it had reduced its export subsidies on sugar. The first sentence of the footnote confirmed that exports of an "equivalent" amount of ACP/Indian sugar were not included in the quantities and outlays reported by the European Communities for the base period level (1986-1990) which served as a basis for the figures set out in the table. Since the footnote applied to the entire entry, the European Communities continued, it applied to both the base outlays and base quantities, thus indicating the basis for the base quantity and outlay levels, in line with the supporting tables which all participants in the negotiations were required to submit.\textsuperscript{202} The first sentence also served to clarify that exports of the quantity of ACP/India sugar imported should not be counted against the commitments made on the base period levels. The second sentence expressed the "average of export" of ACP/India equivalent sugar in the period 1986-1990, which was the base period for the reduction commitments, and was not a simple statement of fact or a narration of particular circumstances.\textsuperscript{203} It indicated that the European Communities was committing itself, as it had done for the other component of its exports of sugar, to limit its exports to a level established on the basis of the exports made in the base period. The European Communities contended that the second sentence, therefore, operated in precisely the same way as the other component of the European Communities' commitments, as it was a limited authorization to provide export subsidies.

4.192 The European Communities further clarified that the first component comprised the commitment levels expressed in the table on export subsidies (which had decreased during the implementation period of the Agreement on Agriculture and had remained fixed since 2001). The second component was the commitment level expressed in the Footnote to the EC's Schedule in respect of ACP/India equivalent sugar, which imposed a ceiling of 1.6 million tonnes (less if the import entitlement was less than 1.6 million tonnes) and a \textit{de facto} budgetary limit of 1.6 million multiplied by the average export refund which could be granted within the first component of the European Communities' commitments. The European Communities argued that the combined

\textsuperscript{201} Appellate Body Report on EC – Computer Equipment, para. 109.

\textsuperscript{202} Exhibit EC–5.

\textsuperscript{203} Appellate Body Report on Canada – Dairy, para. 135. According to the European Communities, the Appellate Body had found that the panel had failed to give meaning to a condition in Canada's goods schedule which the panel had considered was no more than a "description".
operation of these two components meant that, overall, the European Communities had reduced its export subsidies on sugar, over the implementation period. The European Communities asserted that it had respected these limits and provided statistical data in support of that argument.\textsuperscript{204}

4.193 Consequently, when properly interpreted, the footnote was consistent with the Agreement on Agriculture and the European Communities had respected the commitments set out in its Schedule. According to the European Communities, the Complainants had misconceived the footnote and their arguments were premised on the notion that the footnote operated to exclude export subsidies on ACP/India equivalent sugar from any commitments. The Complainants' arguments on the consistency of an exclusion from the Agreement on Agriculture were consequently irrelevant. The European Communities submitted that the articulation of its export subsidy commitments in two components was consistent with each of the provisions of the Agreement on Agriculture cited by the Complainants. Notably, the export subsidies which the European Communities provided to sugar had been subject to reduction commitments in accordance with Article 9.1 (see paragraph 4.186). The European Communities had acted consistently with Article 8 since it had provided subsidies only in conformity with the Agreement (see paragraph 4.185). Furthermore, the European Communities had also provided those subsidies within the limits authorized in its schedule and had thus acted in conformity with Article 8 and Article 3.3 (see paragraphs 4.182 and 4.185).

4.194 The Complainants submitted that the European Communities' interpretation of the footnote was inconsistent, and could not be reconciled, with its ordinary meaning. The words "the Community is not making any reduction commitments" on sugar of ACP or Indian origin, communicated clearly and unambiguously, in their opinion, that the European Communities had not assumed any commitment to reduce export subsidies granted in respect of sugar of ACP or Indian origin. The meaning that the European Communities attributed to the footnote was thus in direct contradiction to its text and indeed rendered the words "not making any reduction commitment" ineffective. They reiterated that, independently of how it was interpreted, the footnote did not constitute a reduction commitment, nor a commitment limiting subsidization, notably with regard to budgetary outlays. In their view, the alleged budget ceiling did not constitute a ceiling commitment as the second sentence simply contained no normative term expressing a commitment, or a term reflecting the idea of a ceiling. Australia, in this context, contended that the reference to an average of 1.6 million tonnes during the base period was not even a factual statement.\textsuperscript{205} First, under its own regime, the EC limited subsidies on exports of sugar of ACP and India origin to a quantity of 1.3 million tonnes of sugar derived from cane or beet harvested in those countries. Secondly, the EC had not disputed that the greater proportion of imports from the ACP countries and India were actually consumed within one EC member State, and were not exported. Third, in response to Australia's question for clarification of statistical data, the EC had acknowledged that it had imported less than 1.6 million tonnes from ACP countries and India during the base period.\textsuperscript{206} The Complainants thus held that, if the European Communities had intended to set out in the footnote one component of a reduction commitment, it would not have used merely descriptive language. Referring to their analysis summarized in paragraphs 4.182-4.186, they sustained that there was no basis in the Agreement on Agriculture for the European Communities' claim that it had the right to make "commitments" to retain export subsidies on a certain quantity of exports, at a ceiling level. As provided for in Article 8 and 3 of the Agreement on Agriculture, and as indicated in the title of Section II of Part IV of a Member's WTO Schedules, export subsidy commitments must be reduction commitments on both quantity and budgetary outlays on scheduled products. The Complainants asserted that Article 9.2(b)(iv) provided further context for the nature of the commitments as reduction commitments.

\textsuperscript{204} Tables 11 and 12 of the European Communities' first written submission.
\textsuperscript{205} Australia's second oral statement, paras. 47–50.
\textsuperscript{206} Australia, in this regard, referred to Annex I of EC's second written submission.
4.195 Even if it were accepted that the footnote indicated the basis for quantity levels for subsidized exports of ACP/India equivalent sugar, the Complainants underlined that the footnote was silent about what values would be multiplied by those quantity levels to arrive at the putative ceiling for budgetary outlays on subsidies on these exports. Further, the alleged "ceiling" had several flaws. First, it could not be found in the text of the footnote or elsewhere in the EC's Schedule of reduction commitments. Second, it did not establish a "ceiling" on these outlays. Third, despite the European Communities' explanations regarding the determination of such ceiling on the basis of the difference between the world market price and the EC intervention price, that difference was not a constant factor. Indeed, to the extent that world market prices have declined over recent years, the average export refund could increase commensurately. Thus, the "ceiling" supposedly imposed by the footnote on the European Communities' budgetary outlays on ACP/India equivalent sugar was not a ceiling at all, but a flexible cap that could increase or decrease based on factors outside the European Communities' control. Thus, far from acting as a ceiling, the budgetary outlays on ACP/India equivalent sugar could be in excess of the levels of budgetary outlays on such sugar during the base period. In this respect, the Complainants found that it was no defence for the European Communities to argue that it "carefully managed" the alleged ceiling (see paragraph 4.222).

4.196 The Complainants sustained that the principle of effectiveness did not require the Panel to endorse an interpretation of the footnote that was devoid of any textual basis.\(^{207}\) The limits to the principle of effectiveness had been observed in GATT and WTO jurisprudence:\(^{208}\) insertions in schedules had repeatedly been declared invalid even though they could have been "interpreted" in a way that gave them legal effect. The Complainants considered that the available jurisprudence was sound because panels and the Appellate Body could not second-guess negotiators and correct their omissions. By contrast, there was nothing in the ruling of the Appellate Body cited by the European Communities to suggest that the principle of effectiveness required panels to go beyond the treaty language.\(^{209}\) Further, an acceptance of the European Communities' effectiveness argument would produce, in the Complainants' view, a completely one-sided result bearing no relationship with the result that reciprocity negotiations would have produced, as the European Communities would achieve unilaterally in its Schedule what could have been achieved only through a negotiated amendment of the Agreement on Agriculture. The Complainants drew an analogy with Annex 5 of the Agreement on Agriculture, as in paragraph 4.211, and argued that, if the European Communities had really wanted to negotiate a similar exemption for ACP/India equivalent sugar from its export subsidy reductions commitments, it could have endeavoured to negotiate with the WTO membership for a framework\(^{210}\) that could accommodate such a result, making counter-concessions, accepting time bound limitations, and any conditions safeguarding the interests of other sugar exporters. For reasons of its own, the European Communities had chosen not to negotiate such an exemption, but had inserted unilaterally a statement in its Schedule purporting to exempt it from its obligations under the Agreement on Agriculture. The Complainants contended that the European Communities was now requesting the Panel to rule that this unilateral exemption had the same legal effect as the negotiated exemptions in the Agreement on Agriculture.


\(^{209}\) Appellate Body Report on Canada – Dairy, para. 134. In that instance, the Appellate Body had concluded that the particular language contained in Canada's Schedule was not descriptive but defined the scope of Canada's concession.

\(^{210}\) Thailand noted that no such framework existed, as the Modalities Paper did not permit any exemptions from export subsidy reduction commitments.
4.197 Thailand also referred to the principle of "contra proferentem" to argue that the European Communities prepared, and inserted, the footnote in its Schedule for its own benefit.\textsuperscript{211} Thailand explained that, unlike tariff concessions which were inserted in the schedules after a negotiated and reciprocal exchange of concessions, the export subsidy reductions commitments were inserted in the schedules unilaterally and their consistency with the guidelines set out in the Modalities Paper was checked in the verification process. Thus, even if the factual statement about the amount of past subsidized exports were "interpreted" to constitute a commitment to observe a ceiling on the future subsidization of those exports, that meaning would not be the preferred meaning according to the "contra proferentem" principle. Thailand held that this principle was a fortiori applicable if the meaning that was least to the advantage of the party which prepared or proposed the provision was the meaning which that party had consistently acknowledged in the past. In this regard, the European Communities' present position was inconsistent with its prior statements as well as its prior practice.

4.198 The Complainants took issue with the inconsistency between the interpretation now advanced by the European Communities and its prior statements before the Committee on Agriculture.\textsuperscript{212} Before this Panel, the European Communities had stated that "[t]he EC has subjected all subsidies on sugar to reduction commitments"\textsuperscript{213}, "[i]t is quite clear that export subsidies which the EC provides to sugar have been subject to reduction commitments in accordance with Article 9.1", and in paragraph 4.222, the European Communities asserted that it could not distinguish between different types of sugar. However, the European Communities also argued that its commitment with respect to the ACP/India "equivalent" sugar was a "ceiling", not a "reduction commitment." To the extent that the European Communities argued that the 1.6 million tons of ACP/India "equivalent" sugar must be added to the European Communities' actual reduction commitments, then the European Communities' overall reduction of sugar subsidies was inconsistent with Article 9.2(b)(iv).

4.199 The European Communities' present position was also inconsistent with its practice of not notifying export subsidies of ACP/India equivalent sugar. If the European Communities had been of the view that it had assumed export reduction commitments in respect of sugar of ACP and Indian origin, it would have provided statistics on the export of such sugar in its notifications.\textsuperscript{214} Assuming that the interpretation submitted by the European Communities were correct, and that, as stated, it had sought to ensure compliance with its commitments under the WTO, the Complainants sustained that the European Communities had in fact failed to respect those commitments when it invoked the flexibility of Article 9.2(b) in marketing years 1997-1998 and 1998-1999. The Complainants noted that the European Communities had not attempted to reconcile its assertions before the Committee on Agriculture with the claims it now submitted to the Panel, explaining why it did not notify the exports of sugar that it claimed to be covered by its reduction commitments, clarifying how it could have observed the requirements of Article 9.2(b) during the implementation period even if its reinterpretation were correct. The Complainants noted that the European Communities had not

\textsuperscript{211} R. Jennings and A. Watts (eds.), Oppenheim's International Law, 90th ed. (Longman, 1992), Vol. I, p. 1279. Thailand noted that this principle was a supplementary means of interpretation recognized in international law, according to which, if two meanings are admissible, the meaning should be preferred "which is least to the advantage of the party which prepared or proposed the provision, or for whose benefit it was inserted in the treaty."

\textsuperscript{212} Exhibit COMP-21, G/AG/R/17, p. 29: "As indicated in footnote 1 of the table on export subsidies contained in Part IV, Section II of Schedule CXL, the EC is not undertaking any reduction commitment on exports of ACP or Indian sugar. Consequently, any financial assistance is not reported to the WTO. For information, these exports amount to approximately 1.6 million tonnes per year."; see also G/AG/R/15, p. 59: "exports of ACP and India sugar are eligible to receive export refunds. As mentioned in the EC's Schedule no reduction commitment is made on this category of sugar."

\textsuperscript{213} European Communities' oral statement at the first substantive meeting of the Panel, para. 31.

\textsuperscript{214} Exhibit COMP-17 (statement included in the notifications indicating that the EC is not notifying the export subsidies granted to sugar of ACP and Indian origin); G/AG/R/34 pp. 3-4; G/AG/R/35 pp. 30. See also footnote 211 above.
submitted any notifications to the Committee on Agriculture relating to the export of ACP/India equivalent sugar and indeed had refused to provide this information, notably when requested by Australia.

4.200 In this context, the Complainants underlined the approach adopted by the Appellate Body in Korea – Various Measures on Beef in reaching a conclusion on the interpretation of Korea's Schedule, "after examining Korea's subsequent statements before the Committee on Agriculture and Korea's annual notifications to that Committee."\(^{215}\) In their view, this implied that, in interpreting a commitment assumed by a Member under the Agreement on Agriculture, a panel could also take into account the interpretation of that commitment advanced by the Member in statements before the Committee on Agriculture or implied in its notifications to that Committee. The Complainants suggested that the Panel rely also, in the present case, on the European Communities' statements before the Committee on Agriculture, and its annual notifications, as a supplementary means of interpretation.

4.201 The Complainants thus considered that the Panel needed to determine the proper interpretation of the footnote and its implications for the resolution of the present dispute. However, independently of how it was interpreted, the footnote could not have the legal effect of exempting export refunds granted to ACP and India equivalent sugar from reduction commitments. Any interpretations would ultimately lead to the same legal result, namely that the export refunds granted to ACP/India equivalent sugar were inconsistent with the Agreement on Agriculture and the SCM Agreement. The Complainants sustained that, if the Panel concluded that the footnote purported to exempt exports of sugar of ACP or Indian origin from the European Communities’ export subsidy reduction commitments, then the Panel would have to declare the footnote without legal effect because it diminished the European Communities’ obligations under Articles 3.3 and 9 of the Agreement on Agriculture.

4.202 Thailand noted that, in the alternative, the Panel may conclude that the footnote indicates that "sugar of ACP or Indian origin" was not to be considered a scheduled product for the purposes of analysing the European Communities' commitments. This interpretation could be based on the fact that the footnote qualified the entry "sugar" in the EC's Schedule. As such it indicated that the term "sugar" "does not include" the quantity of sugar specified in the footnote. If this included "sugar of EC origin of a quantity equivalent to the sugar imported from the ACP countries or India" then it followed that this ACP/India equivalent sugar was not included in the EC's Schedule (assuming such a division could be made under the Agreement on Agriculture). For these reasons, the footnote could also be interpreted to remove this sugar from the EC's Schedule altogether. Thailand noted that this interpretation would be based on the terms of the footnote and would give legal effect to it. Under Article 3.3 of the Agreement on Agriculture, export subsidies listed in Article 9.1 of the Agreement may not be granted to an unscheduled agricultural product. If the footnote was interpreted to remove ACP/India equivalent sugar from the EC's Schedule, export subsidies could not be granted on that sugar at all. Therefore even on this interpretation, Thailand contended that the European Communities would be exceeding its export subsidy reduction commitments for sugar.

4.203 Recalling their reasoning in paragraphs 4.181–4.186, the Complainants countered that the European Communities' interpretation of the footnote conflicted with the distinct requirements under the Agreement on Agriculture. Also, there should be no conflict between Article 3.3 and Article 8. If the "commitments as specified" in a Member's Schedule did not conform to the Agreement on Agriculture, then the Member was not in compliance with the first prong of Article 8. Thus, Article 8 incorporated, in their view, the principle of the US – Sugar Waiver\(^ {216}\) and EC – Bananas III\(^ {217}\) into the

\(^{215}\) Appellate Body Report on Korea – Various Measures on Beef, paras. 103-105.
\(^{216}\) GATT Panel Report on US – Sugar Waiver, paras. 5.2-5.3.
Agreement on Agriculture, in that it required that Schedules and any footnotes therein conform to the Agreement, and did not diminish the European Communities' obligations under that Agreement. If the conflict could not be resolved by way of interpretation through Articles 31 and 32 of the Vienna Convention, a choice had to be made in such a way that the fundamental, multilaterally negotiated provisions prevailed over a unilaterally inserted footnote to a Member's Schedule. The approach taken by the Appellate Body and panels, as outlined in paragraph 4.188, served to support this principle. This principle was equally valid for the market access concessions and commitments for agricultural products contained in the Schedules annexed to the GATT 1994, and was confirmed by paragraph 3 of the Marrakesh Protocol. In the Complainants' view, the footnote clearly sought to diminish specific obligations placed upon the European Communities by Article 9.1 of the Agreement on Agriculture. Australia underlined that the Uruguay Round schedules were prepared with the full knowledge of the US – Sugar panel report, which was adopted in June 1989. Thailand noted that under Article 3.1 of the Agreement on Agriculture the "domestic support and export subsidy commitments" contained in Part IV of a Member's Schedule of Commitments are made an integral part of the GATT 1994. Therefore, the footnote becomes an integral part of the GATT 1994 only to the extent that it constitutes an "export subsidy commitment". For the reasons given above, however, the footnote does not express an export subsidy reduction commitment.

4.204 The European Communities sustained that its interpretation of the footnote was consistent with its wording. Further, the European Communities had consistently interpreted the footnote in the same manner since 1995, based on the application of the Vienna Convention rules of interpretation. The legal effect of the first sentence was to announce that the European Communities had not included, in the base data on which it would apply the percentage reductions set out in the Modalities Paper, ACP/India equivalent sugar. In so doing, the European Communities had transferred this portion of its exports from the part of its commitments articulated in the table, to the part of its commitments articulated in the footnote. The first sentence stated that the European Communities was not taking reduction commitments on ACP/India equivalent sugar, meaning that the European Communities did not reduce, in annual instalments, the level of export subsidies on that portion of its exports. The first sentence therefore had legal effect, in the European Communities' view. However, this did not mean that the European Communities had not undertaken to limit subsidization, or that the European Communities did not make reduction commitments, or that the European Communities had not reduced the maximum scheduled export subsidies on an annual basis in its schedule.

4.205 While the European Communities agreed that the second sentence was a factual statement, it disagreed with the view that it contained no normative term expressing a commitment. Rather, it needed to be interpreted in its context. In this regard, the European Communities regarded two elements as being relevant context: the EC's Schedule of export subsidy commitments, to which the footnote was attached, and which contained several factual statements with, what the European Communities held was normative effect; and the first sentence of the footnote. Because the European Communities was not subjecting that portion of its exports to the coefficients set out in the Modalities Paper, the European Communities considered that it did not have to schedule the diminishing commitment levels, but rather that it was enough to set out the commitment level within which the European Communities was to limit the volume of exports subsidized. The European Communities sustained that the second sentence set a limit in the same way as base periods for all other products. However, while other base periods were the starting point from which the maximum level of

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219 The European Communities indicated that in that table it had set out figures representing the base period levels, which provided the basis from which the limited authorization to provide export subsidies was subjected to gradual reduction. The second sentence of the footnote was intended to have an "equivalent" effect, i.e., to establish the European Communities' commitment level in respect of the separately articulated commitment on ACP/India 'equivalent' sugar.
subsidized exports was reduced, this base was not to be reduced, and was therefore to act as a fixed ceiling.

4.206 Turning to the Complainants' contentions regarding the absence of budgetary outlay commitment in the footnote, the European Communities sustained that Article 3.3 incorporated the export subsidy commitments into the GATT, but did not prescribe any form for such commitments. Since the European Communities considered that it had respected the commitments it had undertaken to limit subsidization on A/B sugar and ACP/India equivalent sugar, it had acted consistently with Article 3.1. Moreover, since the European Communities had not provided export subsidies in excess of the commitment levels set out in its schedule, it had acted consistently with Article 3.3. Here, the European Communities recalled the operation of its commitments on exports of A/B sugar as imposing a de facto budgetary limit. Moreover, in the European Communities' opinion, Article 3.3 did not impose an obligation to have both a budgetary outlay and a quantity commitment level, but merely referred to the "commitment levels specified therein". Article 3.3 only set out the obligation to provide Article 9.1 listed subsidies in conformity with the commitments specified in a Member's schedule. The obligation to schedule both types of commitments was only set out in the paragraph 11 of the Modalities Paper, of which, the European Communities recalled, the footnote was a negotiated departure.

4.207 The European Communities also submitted that participants in the Uruguay Round could negotiate departures from the reduction formulae agreed in the Modalities Paper, and that the footnote constituted one such departure. The European Communities contended that in the absence of any express indication to that effect, such departures could not be presumed. Consequently, it could not be assumed that, without having being requested to do so by any other Member, the European Communities undertook voluntarily reduction commitments well in excess of those agreed as part of the Modalities Paper. In this context, the European Communities argued that it was not alone in negotiating such departures. New Zealand did not specify any quantitative limits in its schedule, and only scheduled reductions in budgetary outlays. Australia had sub-divided the category "other milk products" into two categories, fats and solid non-fats (which were not listed in the Modalities Paper), specifying separate quantity commitments, while indicating a budgetary outlay commitment only on the general product. The European Communities alleged that there was nothing to distinguish such commitments from the footnote. The European Communities also submitted that the Modalities Paper explicitly foresaw that it might not be possible to schedule quantitative limitations, particularly in respect of incorporated products. As for the footnote, only one set of commitments was scheduled for these products. Since, in the European Communities' view, the Complainants had failed to establish that the footnote was inconsistent with the Agreement on Agriculture, consequently, the footnote itself could not be regarded as inconsistent with Article 8. With respect to Article 9.1, the European Communities recalled that, because it did not wish to reduce its commitment levels for sugar, it had negotiated a departure from the Modalities Paper in its Schedule, in the form of the footnote. The European Communities considered, however, that it had subjected the maximum amount of export subsidies it granted to exports of sugar to reduction commitments over the implementation period, and that, consequently, it had also acted consistently with Article 9.1. Concerning Article 9.2(b), the European Communities submitted that it was not before the Panel, and had lapsed (see Section B.1, Terms of reference). It was therefore irrelevant to the matter before the Panel.

4.208 The European Communities challenged Thailand's invocation of the principle of contra proferentem, arguing that this principle had seldom been referred to in international law instances

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220 See Part IV, Section II of New Zealand's Schedule (XIII).
221 See Part IV, Section II of Australia's Schedule (I).
since the early 1930s,\textsuperscript{222} due to its imprecise nature and scope. That principle could not be used in the present case since, in particular, doubts had been cast on it.\textsuperscript{223} The European Communities raised questions as to the applicability of this principle to a multilateral treaty, and as to how it fitted into the Vienna Convention, which was, in the European Communities' opinion, based on the principle of good faith. The European Communities regarded the principle of \textit{in dubio mitius} as more appropriate, since it applied to treaties, had been recognized by the Appellate Body, and required that an interpretation be preferred which impinged as little as possible on the sovereignty of Members.\textsuperscript{224} According to the European Communities, in the present case, this would imply interpreting the footnote as setting a ceiling in order to allow the European Communities to continue to provide export subsidies on this portion of its exports.

4.209 The Complainants contended that the European Communities had drawn a number of false analogies in support of its contention that an export subsidy commitment needed not contain a budgetary outlay commitment level. First, Australia’s scheduling of milk products involved both budgetary outlay and quantity reduction commitments, with specific quantity limits set for two sub-groups of milk product, a form of scheduling which was expressly envisaged by paragraph 8 of Annex 8 of the Modalities Paper. On the other hand, a form of scheduling based on a quantity of the same product was never envisaged. The specific quantity limits for the product sub-groups served to impose tighter disciplines on quantities of "particular products" which might be exported than an overall reduction limit for a group of products. Secondly, New Zealand had scheduled the elimination of all export subsidies on all covered products by the end of the implementation period, and actually eliminated the export subsidies in question in 1994/1995. New Zealand had clarified to the Committee on Agriculture, in response to a question from the European Communities, that it had not been possible to identify the product-specific quantities of subsidized exports for the base period, as the historical taxation arrangements were non-product specific.\textsuperscript{225} Thirdly, the European Communities had also drawn a false analogy with the incorporated products category, which comprised a diverse range of highly processed agricultural products and basic products incorporated into the processed products. Again, paragraph 9 of Annex 8 of the Modalities Paper specifically envisaged that the reduction commitment for incorporated products could be expressed in terms of aggregate budgetary outlays. Moreover, the present case did not concern export subsidies granted to incorporated products, accordingly the form of export subsidy commitment envisaged under the Modalities Paper for this type of subsidy was irrelevant. The Complainants considered that the European Communities' novel proposition found no support in the Agreement on Agriculture. Article 3.3 prohibited granting subsidies in excess of budgetary outlay and quantity commitment levels. Similarly, Articles 9.2(a) and 9.2(b) had been drafted on the assumption that there were both a budgetary outlay commitment and a quantity commitment for all scheduled agricultural products. The Complainants submitted that, if an export subsidy commitment could take any form, these provisions would have been drafted differently.

4.210 The Complainants held that the European Communities' contention that the footnote represented a negotiated departure from the Modalities Paper, lacked any foundation. There was no bargaining over the footnote, and no compensation elsewhere in the WTO agreements for the departure from the European Communities' commitments under the Agreement on Agriculture allegedly contained in the footnote. Citing \textit{Korea – Various Measures on Beef}, the Complainants held that there was no official record that the terms of the footnote were specifically "agreed" to by the

\begin{thebibliography}{9}
\bibitem{222} The European Communities pointed to the reference to \textit{Oppenheim's International Law} in footnote 58 to Thailand's second written submission; and McNair.
\bibitem{225} G/AG/R/2 and G/AG/R/3.
\end{thebibliography}
Complainants, or any other WTO Member, prior to the completion of the Uruguay Round, and there was no record of the nature of the compensation received. Also, by contrast with Korea – Various Measures on Beef, there was no ambiguity over the ordinary meaning of the European Communities' footnote. Resorting to negotiating history, or to the Modalities Paper, as suggested by the European Communities in paragraph 4.193 would therefore serve no purpose.

4.211 Moreover, the Complainants noted that the European Communities did not cite the relevant provision of the Modalities Paper that would have permitted it to adopt a lesser obligation than that expressed in the language of paragraphs 11 and 12 of that text.\(^{226}\) In their view, the reduction commitments were multilateral in nature and did not constitute negotiated concessions. Unlike the market access commitments, they were "self-contained" in regard to the balance of concessions, since they were not made contingent on concessions in other areas of the agriculture negotiations.\(^{227}\) Paragraph 7, in particular, did not lend support to the notion that "ACP/India equivalent" sugar might be distinguished from other quota sugar within a quantitative category. Further, there was no provision in the Agreement on Agriculture which provided for lesser reduction commitments for developed WTO Members in respect of any product or sub-category of a product. In the export competition area, there was no multilateral cover, comparable to Annex 5 of the Agreement on Agriculture, which was negotiated, and paid for, by additional undertakings, in the market access area.

4.212 The European Communities dismissed the allusion to Annex 5 of the Agreement on Agriculture as an example of a negotiated exemption as irrelevant. While the footnote was a departure from the Modalities Paper, it was not a departure from the Agreement on Agriculture. Annex 5, by contrast, constituted a departure from the Agreement on Agriculture. Further, Annex 5 provided an exemption to the Agreement on Agriculture which had been open to all WTO Members, whereas the footnote was a negotiated departure from the Modalities Paper specific to one Member. The European Communities found it therefore logical that a general exemption appeared in the Agreement, and that specifically negotiated treatment should appear in the schedule of the Member concerned. The European Communities suggested that the Members who utilized Annex 5 had "paid" for it in exactly the same way that the European Communities had "paid" for the footnote, i.e. in the general balance of rights and obligations negotiated in the Uruguay Round.

4.213 In response to the Complainants' analysis summarized in paragraphs 4.181–4.187, the European Communities submitted that the conclusion regarding the consistency of the footnote with the Agreement on Agriculture could be reached without creating a conflict between the provisions of the footnote, or those of the Agreement on Agriculture, as alleged by the Complainants. According to the European Communities, the Panel was not obliged to declare the footnote, which was part of a validly concluded treaty, invalid. The European Communities noted that under general public international law, one part of a treaty could rarely render another part of the same treaty without legal effect. The WTO Agreement specifically recognized such a possibility: (a) the general interpretative note to Annex 1A established a hierarchy between the other Annex 1A Agreements and GATT 1994; (b) Article XVI.3 of the WTO Agreement established a hierarchy between the WTO Agreement and the Annex 1A Agreements; (c) Article 1.2 of the DSU had a similar logic. Further, the US – Sugar Waiver case established that, on the basis of the specific wording of Article II.1 of the GATT 1947, its object and purpose, a GATT Contracting Party could not derogate, in its schedule, from other obligations. The European Communities expressed doubt whether that case-law could be transposed to Article 3 of the Agreement on Agriculture, since the panel had largely based its reasoning on the terms of Article II.1 of the GATT 1947, involving market access "concessions", as compared to export subsidy "commitments". The European Communities also questioned the basis on which the

\(^{226}\) Exhibit COMP-19.

\(^{227}\) The Complainants pointed out that, in the export competition section of the paper, there were no counterpart provisions to paragraph 6 dealing with expansion of current access, which allowed for due account to be taken of reduction commitments in the export competition area.
Complainants would have the Panel derogate from some of the fundamental principles of international law. The European Communities believed that the Panel would not, in any event, need to address this issue because, when properly interpreted, the footnote could not be considered to conflict with the Agreement on Agriculture.

3. Application of the footnote to "ACP/India equivalent sugar"

4.214 The Complainants submitted that the terms of the reservation made by the European Communities in its Schedule of Concession did not cover ACP/India equivalent sugar. By failing to comply with the text of the footnote, the European Communities was acting inconsistently with Articles 3.3, 8 and 9.1 of the Agreement on Agriculture. A finding that the terms of the footnote did not cover the subsidies at issue would not ensure a fully satisfactory resolution of the dispute. The issues arising from the terms of the footnote were subsidiary issues that the Panel should address only if it were to conclude that the footnote was legally valid.

4.215 Referring to the European Communities' contention that the footnote excluded from the scope of its reduction commitment a quantity of sugar that was merely equivalent to the quantity of sugar that it imported from ACP countries and India, the Complainants submitted that the terms of the footnote applied exclusively to exports of "sugar of ACP and Indian origin". The footnote thus contemplated exclusively the re-export of sugar of ACP or Indian origin. In this respect, the Complainants noted the European Communities' explanations to the effect that it could not distinguish whether the exported white sugar was produced from the same raw sugar that was imported and that there were no dedicated facilities for refining this imported sugar. In the Complainants' view, it was thus clear that the exported sugar was not processed from the imported raw sugar. Moreover, the footnote did not mention, and could not be interpreted to cover, "equivalent" exports. Thus, even if the Panel were to find that Members could exempt themselves from their obligations under the Agreement on Agriculture by inserting footnotes in their Schedules of Concessions, the Panel would have to conclude that the footnote inserted by the European Communities did not exempt it from those obligations in respect of quantities of sugar equivalent to sugar of ACP and Indian origin.

4.216 The European Communities replied that this issue constituted a separate claim which had not been properly stated in the panel requests (see Section IV.B above, Terms of reference). As part of its argumentation on good faith, the European Communities submitted that the footnote covered refunds on exports equivalent to imports and that the Complainants were aware of this fact during the Uruguay Round.

4.217 The European Communities sustained that it was well known to all parties, at the time of the conclusion of the WTO Agreement, that the European Communities did not grant export refunds only on the re-export of sugar originally of ACP and Indian origin, but to a quantity equivalent to such exports. According to the European Communities, this was reflected in the drafting of the footnote which referred to the "average of export" as being 1.6 million tonnes. The European Communities argued that this was a reference to exports which were not ACP/India raw sugar imported, refined, and subsequently exported, but rather the equivalent quantity of ACP/India sugar that had been imported. The European Communities sustained that the term "export" in "average of export" had the same meaning as "exports" in the first sentence. In the European Communities' view, the footnote

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228 Exhibit COMP-1, (2001/C 50/01) pp. 23-24, 27 and 29; Exhibit COMP-21.
229 Report of the Working Party on European Communities – Refunds on Exports of Sugar, adopted on 10 March 1981, BISD 28S/80, para. 35: "As was well known, the EEC imported 1.4 million tons per year or ACP raw sugar at guaranteed prices and exported an equivalent amount of white sugar." The European Communities submitted that both Australia and Brazil participated in the Working Party, and that Australia was clearly aware of the fact that not all imports of ACP/India were re-exported. In para. 34 of the Working Party report, it is noted that: "The representative of Australia also stated that most ACP sugar went to the United Kingdom market and was refined and consumed there."
therefore covered refunds on exports equivalent to imports. Second, the European Communities had
made its intentions clear in two letters, when submitting draft schedules and associated documents to
the negotiating group\(^{230}\), reiterating its objective to have the footnote adopted by the other negotiating
parties. Since the footnote was adopted as proposed, the European Communities submitted that these
cover letters were equally relevant in establishing the meaning of the footnote, i.e. that it covered
exports "corresponding" to imports.

4.218 The Complainants reaffirmed that the scope of application of the footnote was a subsidiary
argument supporting their legal claim that the European Communities was exceeding its export
subsidy reduction commitments. They sustained that the words "ACP and Indian origin" needed to be
interpreted in accordance with the ordinary meaning of "origin" to mean sugar that came from the
ACP countries or India. They registered the European Communities' recognition, in paragraph 4.217,
that it exported an amount of sugar "equivalent" to the amount it imported from ACP countries and
India, and that may actually be of domestic origin. They noted, however, that the amount of sugar
exported was not equivalent to the amount of sugar imported under the preferential arrangements\(^{231}\),
but was set at an arbitrary limit based on preferential imports plus, presumably, Special Preferential
Sugar (SPS), despite the fact that SPS was not eligible for export refunds. Even assuming that the
footnote was a legitimate derogation from the Agreement on Agriculture, the Complainants argued
that the export of an "equivalent" amount of EC sugar was not what was provided for.

4.219 Thailand highlighted a discrepancy in the arguments presented by the European
Communities before the Committee on Agriculture\(^{232}\), where the European Communities had
confirmed that export subsidies were granted only to processed sugar obtained from ACP and Indian
sugar, and its standpoint in paragraph 4.217 where the European Communities interpreted the
footnote as applying to sugar of EC origin that was "equivalent" to sugar imported from the ACP
countries and India. Referring to the European Communities' arguments with respect to
circumstances supposedly "well-known" to the participants in paragraph 4.217, the Complainants
considered that what was at issue was treaty text. The arguments presented by the European
Communities were not based on an analysis of the terms of the treaty, considered in light of context
and the object and purpose. The cover letters cited by the European Communities did not
unambiguously support its interpretation, as the letters did not refer to "sugar of EC origin", but rather
to sugar that "corresponds" to imports from ACP countries and India. According to the Complainants,
this phrase could refer to sugar refined from raw sugar imported from the ACP countries and India
rather than EC quota sugar.

4.220 The European Communities recalled its argumentation that this claim was not within the
Panel's terms of reference. However, should the Panel find that the question of interpretation of the
terms of the footnote fell within its terms of reference, the footnote should be interpreted as permitting
the export of a volume of subsidized exports "equivalent" to the volume of imports of ACP and Indian
origin. Referring to its explanations relating to the interpretation of the footnote, and those relating to
the consistency with the Agreement on Agriculture, the European Communities reiterated that the
figure represented by the word "export" in the second sentence of the footnote did not, in the
knowledge of all Members, refer to re-export of ACP or Indian sugar, but rather to an amount
"equivalent" to the total volume of imports from those countries. To the extent that recourse to
supplementary means of interpretation may be of assistance, the European Communities submitted
that the preparatory work, and the circumstances of conclusion, confirmed that the European
Communities' interpretation was the meaning intended by the parties. The European Communities
had already noted that in the letters transmitting the draft schedule to the GATT Secretariat, the

\(^{230}\) Exhibit EC-5 and Exhibit EC-6.
\(^{232}\) G/AG/R/15, p. 59.
European Communities had made it clear that it considered that the footnote covered a volume of exports corresponding to the volume of imports from ACP countries and India.

4.221 The European Communities confirmed that it granted export subsidies on exports of sugar "equivalent" to the amount of imports which could be imported from ACP countries and India, up to a maximum of 1.6 million tonnes, although both the import entitlement and the actual imports were frequently substantially more than 1.6 million tonnes. Where the amount of import entitlement was lower than 1.6 million tonnes, that amount operated as the ceiling. The European Communities submitted statistical data in support of the view that it considered and treated the 1.6 million tonnes as a cap on the amount of exports which could benefit from export subsidies as ACP/India equivalent sugar.

4.222 Under Regulation No. 1260/2001, the European Communities continued, the competent authorities were authorized to grant export refunds only to the extent that there was a difference between world market and Community prices. They could not distinguish between different "types" of sugar. The European Communities authorities had limited control over the evolution of the amount of individual refunds. The Commission verified on a weekly basis that the export refunds granted remained within the limits set out in the WTO Agreement, by way of a control sheet used to track the volume of sugar for which export licences had been issued, and establishing a running total of volume and outlays, and the average export refund. These figures were then compared to the total of the two component limits of the European Communities’ export subsidy commitments: its standard commitments (1,273,500 tonnes and €499,100,000) and its ACP/India equivalent commitments (1,600,000 tonnes and 1,600,000 multiplied by the average export refund). Through this tender system, the European Communities managed its export refunds in order to respect its export subsidy commitments under the WTO.

4.223 The European Communities reaffirmed that the footnote was a negotiated commitment and was part of the complex balance of rights and obligations set out in the WTO Agreement, the individual agreements annexed to it, and the schedules of Members which were an integral part of the Agreement. The European Communities continued to respect that obligation which required it to export onto the world market. The European Communities sustained that since the early 1980s, it had consistently argued that the portion of its exports "equivalent" to its imports from ACP and India should be entitled to differential treatment. This differential treatment, in its view, was articulated in the footnote, a commitment which the European Communities claimed to have negotiated, and paid for, in the Uruguay Round negotiations, including with the Complainants. The footnote was also a derogation from the Modalities Paper. The European Communities asserted that its interpretation of the footnote was consistent with its own objectives and those of other WTO Members, in negotiating the footnote. The European Communities held that the Appellate Body had made it clear that a treaty interpreter could not lightly assume that a WTO Member projected no demonstrable purpose on a specific provision.

4.224 The European Communities considered that Australia, in the documents it had submitted to the Panel, had admitted that it shared the European Communities' understanding of the footnote. For instance, the G8 "Record of discussion" evidenced Australia's understanding of the European Communities' intention to reduce only that portion of its export subsidies corresponding to "net

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233 Note by the EC: under the ACP Sugar Protocol, the EC-India Agreement on sugar and as special preferential sugar. Fluctuations are typically brought about by changes to the amount of sugar which can be imported as special preferential sugar.

234 Table 10 of the European Communities' first written submission.

235 Exhibit EC-16.

exports.” More explicitly in the European Communities’ view, the Australian memorandum on “Issues still requiring settlement” of 31 January 1994 referred to export subsidies covered by the footnote as those “corresponding to [the EC’s] imports of sugar from ACP countries and India.” Given that Australia was the only Complainant who directly negotiated the footnote with the European Communities and was the only WTO Member (with the exception of the ACP countries and India) who discussed the footnote with the European Communities, the European Communities submitted that Australia’s understanding of the footnote was highly probative of the parties’ intentions in adopting the footnote.

4.225 **Australia** contested the European Communities’ allegation that it had negotiated special exceptions from its WTO export subsidy reduction commitments for sugar, and noted that the European Communities could not cite any provision in the Modalities Paper – let alone any of the WTO agreements – for what it has described as an entitlement to differential treatment, a treatment more favourable than that accorded to developing country sugar exporters under the provisions of the Agreement on Agriculture. There was no document signifying agreement by any participant in the Uruguay Round that the European Communities should enjoy differential treatment. In signing on to the Final Act embodying the results of the Uruguay Round, the European Communities undertook to ensure the conformity of its laws, regulations and administrative procedures with its obligations as provided in the annexed Agreements to the WTO Agreement. It also accepted the treaty obligation that no reservations may be made in respect of any of the provisions of the Multilateral Trade Agreements, except to the extent provided for in those Agreements. There was nothing in the Agriculture or SCM Agreements that permitted the European Communities to “grandfather” pre-existing measures inconsistent with its WTO obligations for sugar export subsidies. Australia further confirmed that it had raised this inconsistency with the European Communities during the Uruguay Round, pointing out that the footnote would be open to challenge.

4.226 The **European Communities** submitted, in the alternative, that, should the Panel first disagree with the European Communities’ interpretation of its commitments with respect to ACP/India equivalent sugar and second, agree with the Complainants that the footnote constituted an inoperative exclusion from the European Communities’ obligations under the Agreement on Agriculture, that the Panel should nevertheless reject the Complainants’ claims for the following reasons. By agreeing to the European Communities’ proposed treatment of ACP/India equivalent sugar, and bringing this challenge subsequently, the Complainants would have the European Communities reduce the exports provided from 1.6 million tonnes to zero, rather than 1,264,000 tonnes, as would have been the case if the 1.6 million tonnes had been reduced by 21 per cent, effectively requiring the European Communities to reduce the base quantity of subsidized exports by 60 per cent instead of 21 per cent. The European Communities therefore submitted that the Complainants exercised unreasonably their rights, were estopped from bringing this claim, acted inconsistently with the principle of good faith and Article 3.10 of the DSU, and that they should agree to the correction of the European Communities’ scheduling commitments. The European Communities indicated that the arguments set out with respect to C sugar applied, mutatis mutandis, to the Complainants’ claims in respect of ACP/India equivalent sugar. (See also paragraph 4.217)

4.227 The European Communities drew an analogy with tariff concessions, submitting that export commitments were the subject of detailed negotiations, and that the EC commitments represented the

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237 Exhibit ALA-3.
238 Exhibit ALA-8.
239 Article XVI:4 of the WTO Agreement.
240 Article XVI:5 of the WTO Agreement.
241 Exhibit ALA-3.
negotiated balance of the varied interests of all participants in the Uruguay Round. The European Communities submitted that, in challenging the European Communities' footnote, the Complainants were trying to alter that balance. The European Communities considered that it was only normal that importing Members defined their offers (and their ensuing obligations) in terms which suited their needs. On the other hand, exporting Members had to ensure that their corresponding rights were described in such a manner in the Schedules of importing Members that their export interests, as agreed in the negotiations, were guaranteed. According to the European Communities, a special arrangement was made for this purpose in the Uruguay Round, and a process of verification of tariff schedules took place from 15 February through 25 March 1994, which allowed the participants to check and control, through consultations with their negotiating partners, the scope and definition of tariff concessions. The fact that Members' Schedules were an integral part of the GATT 1994 indicated that, while each Schedule represented the tariff commitments made by one Member, they represented a common agreement among all Members. The European Communities held that the claims which the Complainants made in these proceedings should have been raised during the verification process, and if considered valid, the Members concerned could have negotiated a different balance of concessions.

According to the European Communities, the Complainants were aware, by virtue, inter alia, of the inclusion of the footnote in the European Communities' export subsidy commitments, both in its draft and final form, of the existence of the European Communities' intended treatment of ACP/India equivalent sugar. The European Communities contended that, in 1981, the Complainants had argued against ACP equivalent sugar being treated separately from other export refunds on EC sugar. In 1993 and 1994, the Complainants explicitly agreed to the compartmentalized treatment of ACP/India equivalent sugar in negotiating and concluding the WTO Agreement. The elements on which the Complainants based their challenge in this dispute were in existence at the time of conclusion of the Uruguay Round.

With respect to ACP/India equivalent sugar, the Complainants rejected the European Communities' claim that they were estopped from bringing their complaint, and that they implicitly agreed to the footnote in the EC's Schedule. The Complainants indicated that their rebuttal on good faith and estoppel for C sugar (see Section IV.D.3(b) above) applied mutatis mutandis to the European Communities' arguments on these matters for ACP/India equivalent sugar.

According to the Complainants, the European Communities had also mistakenly characterized the scheduling of export subsidy reduction commitments as being conducted on a bilateral offer and request basis (see paragraph 4.227). Contrary to the European Communities' assertions, a WTO Member's Schedule of bound tariff concessions was not analogous to the EC's Schedule of reduction commitments for export subsidies for agricultural products. While WTO Members bargained over their tariff concessions, no similar bargaining or negotiation took place over the contents of reduction commitment schedules. To the extent that any analogy to the bargaining of tariff concessions could be found in the Agreement on Agriculture, it was found in the reduction commitment levels provided in Article 9.2, rather than in the individual Member Schedules. A WTO Member that objected to the content of another Member's Schedule of reduction commitments had neither the time nor the opportunity to negotiate further on the contents of the Schedule. The only recourse would have been to decline to sign the WTO agreements altogether or to engage in dispute settlement after the signing of the Uruguay Round Agreements.

The Complainants argued that the Panel could not give legal effect to a unilateral reservation like the European Communities' footnote, without reducing the multilateral agreement on subsidy reduction commitments contained in the Agreement on Agriculture to a voluntary system of unilateral concessions. The Complainants considered that this would have severe consequences for future

negotiations. The closing weeks and days of negotiations would see a flood of footnotes qualifying one previously negotiated commitment after another. WTO Members might never sign the agreements, as they would see negotiated benefits eliminated by footnotes or would simply conclude that they could not be sure what the agreements meant. According to the Complainants, dispute settlement would soon be concerned with interpreting treaty text in light of footnotes, and even one footnote in light of another (see also arguments with respect to C sugar in Section IV.D.3(b) above).

F. ARTICLE 3 OF THE SCM AGREEMENT

4.232 The Complainants submitted that the export subsidies granted in respect of exports of quota sugar, ACP/India equivalent sugar and C sugar were prohibited subsidies under the SCM Agreement. More specifically, the Complainants claimed that the EC sugar regime provided subsidies that amounted to an export subsidy listed in Item (d) of the Illustrative List of Export Subsidies in Annex I of the SCM Agreement (see Section IV.D.2(a) above) and that the export refund on exports of quota sugar and ACP/India equivalent sugar amounted to an export subsidy listed in Item (a) of the same Illustrative List. As such, the European Communities' export subsidies were prohibited under Article 3.1(a) of the SCM Agreement, and by maintaining and granting prohibited export subsidies, the European Communities violated Article 3.2 of the SCM Agreement. Furthermore, Australia and Brazil claimed that the EC sugar regime was also otherwise inconsistent with Article 3.2 of the SCM Agreement.

4.233 The European Communities argued that the SCM Agreement was not applicable to agricultural products, in casu, sugar. It pointed to, inter alia, Article 21.1 of the Agreement on Agriculture and claimed that this provision had been interpreted by the Appellate Body as meaning that the other Annex IA Agreements applied "except to the extent that the Agreement on Agriculture contains specific provisions dealing specifically with the same matter." The European Communities contended that it was clear that the Agreement on Agriculture contained specific provisions dealing specifically with the "same matter". For example, it cited the fact that Articles 3, 8, 9, 10 and 11 of the Agreement on Agriculture set out detailed rules on the provision of export subsidies, thereby permitted them up to a certain level. Specific rules were also set out on the type of subsidies which could be granted, and specific mechanisms were defined on how to deal with possible cases of circumvention. For the European Communities, applying the SCM Agreement to agricultural export subsidies (even those granted inconsistently with the Agreement on Agriculture), and specifically the prohibition on export subsidies, would undermine the specificity of the agricultural regime, and the gradual process of reform which all Members signed up to.

4.234 The Complainants interpreted Article 21.1 of the Agreement on Agriculture to mean that the Agreement on Agriculture and the SCM Agreement applied cumulatively to measures affecting agricultural products. For them, the chapeau to Article 3 of the SCM Agreement, read together with Article 21.1 of the Agreement on Agriculture, set out a special exception for those export subsidies provided in conformity with the Agreement on Agriculture, that is: (a) Article 9.1 listed export subsidies subjected to reduction commitments; (b) Article 9.1 listed export subsidies on scheduled products that were not in excess of the budgetary outlay and quantity commitments specified in the Schedule; and (c) fulfillment of the individual undertakings of each Member in accordance with Article 8 of that Agreement. In the view of the Complainants, the Agreement on Agriculture did not constitute a lex specialis in regard to agricultural products or to measures applied to agricultural products, whether subsidies or any other obligation subject to WTO disciplines. The Agreement on Agriculture and the SCM Agreement were separate treaties, creating separate rights and obligations.

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243 In this section of the Panel report, it should be noted that Australia's claims under the SCM Agreement do not involve all quota sugar, rather the "ACP/India equivalent" component of the A and B quota sugar.

and providing for different remedies. A measure could be inconsistent with one agreement but not with the other, or it could be inconsistent with both. A finding that a measure was inconsistent with both, however, would require proof of different elements.

4.235 In this respect, the Complainants referred to the US-FSC panels and Appellate Body reports which analysed export subsidies granted to agricultural products under both the SCM Agreement and the Agreement on Agriculture. For the Complainants, the relevant provisions of the SCM and the Agreement on Agriculture needed to be read in context and needed to give meaning to the intent of the negotiators to integrate – at least partially – agricultural export subsidies into the SCM Agreement. Here, the Appellate Body had examined the challenged measures under both the Agreement on Agriculture and the SCM Agreement, without any suggestion that to do so in any way undermined Article 21.1 of the Agreement on Agriculture. The Appellate Body, in both the original proceedings and the recourse to Article 21.5, found that the subsidies in that case were not only prohibited export subsidies under Article 3.1(a) and 3.2 of the SCM Agreement but also inconsistent with the export subsidy obligations under Articles 3.3, 8 and 10.1 of the Agreement on Agriculture.

4.236 The Complainants also cited Article 3.1 of the SCM Agreement, which prohibited export subsidies, "except as provided in the Agreement on Agriculture." In Canada – Dairy, the Appellate Body had said that this clause "indicates that the WTO-consistency of an export subsidy for agricultural products has to be examined, in the first place, under the Agreement on Agriculture." If an examination "in the first place" of export subsidies under the Agreement on Agriculture revealed that these subsidies were not "as provided in the Agreement on Agriculture," then an examination "in the second place" was required under the SCM Agreement.

4.237 For the Complainants, there was no inconsistency or conflict between the references in Article 3.1 of the SCM Agreement ("except as provided in the Agreement on Agriculture") and that in Article 21.1 of the Agreement on Agriculture (that provisions of other agreements apply "subject to the provisions of this Agreement"). These two provisions, read together, meant that any subsidy permitted under the Agreement on Agriculture was not subject to the disciplines of the SCM Agreement. However, this reading did not compel or even imply the additional inference drawn by the European Communities that subsidies not permitted under the Agreement on Agriculture were equally not subject to the disciplines of the SCM Agreement. Nothing in the text or, indeed, the object and purpose, of either provision supported such a broad reading of the two provisions. The European Communities’ interpretation of the relationship between these agreements and the limited scope of application of the SCM Agreement in respect of export subsidies granted to agricultural products could not be reconciled with the plain wording of the provisions regulating this matter. The meaning of the terms in the SCM Agreement was unambiguous: "except" where the Agreement on Agriculture provides otherwise, the disciplines set out in Article 3 of the SCM Agreement apply to subsidies on agricultural products.

4.238 The European Communities, in response to the Complainants arguments in paragraph 4.235 in relation to the US – FSC dispute submitted that neither the panel nor the Appellate Body had found that the SCM Agreement applied to agricultural products. The panel had found that the FSC scheme was inconsistent with the SCM Agreement, "except as provided in the Agreement on Agriculture." The panel, however, did not make a finding that, because the FSC scheme was inconsistent with the Agreement on Agriculture, it was subject to and inconsistent with the SCM Agreement as far as

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246 Appellate Body Report on US – FSC, paras. 177(a) and (d). See also Appellate Body Report on US – FSC (Article 21.5 – EC), paras. 256(b) and (d).
agricultural products were concerned. Furthermore, the panel considered it necessary to make separate recommendations under the SCM Agreement and the Agreement on Agriculture. 249 This suggested that the panel considered that the Agreement on Agriculture excluded the applicability of the SCM Agreement with respect to agricultural products. In determining the level of countermeasures under Article 4.10 of the SCM Agreement in the Article 22.6 arbitration in the FSC dispute, the European Communities continued, the Arbitrators took the view that an amount corresponding to the value of the subsidy to agricultural goods should be deducted. 250 The panel clearly understood, therefore, the SCM Agreement as not being applicable to export subsidies granted on agricultural goods.

4.239 The European Communities also noted that there were significant factual differences between the schemes at issue in the FSC dispute and the present dispute, which explained why the Agreement on Agriculture and the SCM Agreement applied concurrently in the FSC dispute, but did not apply cumulatively, as the Complainants would have it in the current dispute 251. As a consequence, the application of the two agreements concurrently in the FSC dispute, did not mean that the two agreements could be applied cumulatively in the present dispute.

4.240 The Complainants responded that this interpretation was not supported by WTO jurisprudence and would serve to void the relevant provisions of the Agriculture and SCM Agreements of any meaning. The Complainants reiterated that Article 3.1 of the SCM Agreement ("Except as provided in the Agreement on Agriculture...") and Article 21 of the Agreement on Agriculture ("The provisions of GATT 1994 and of [other covered Agreements] shall apply subject to the provisions of this Agreement") were straightforwardly consistent and complementary. If a subsidy was permitted or exempted from action under the Agreement on Agriculture, the SCM Agreement did not apply to that subsidy. If a subsidy was not permitted or exempted from action under the Agreement on Agriculture, the SCM Agreement did apply. Finally, the Complainants contended that if the drafters of the SCM Agreement had intended that the SCM Agreement should not apply to agricultural products at all, it would have been simple to have inserted a provision to that effect. However, no such provision existed. On the contrary, for the limited timeframe of the implementation period, the Peace Clause of the Agreement on Agriculture indicated that only those export subsidies that fully conformed to the provisions of the Agreement on Agriculture on export subsidies were exempted from actions under the SCM Agreement. The logical implication of this provision was that export subsidies that did not conform fully to the Agreement on Agriculture were not exempted from actions under the SCM Agreement.

4.241 The European Communities, referring to the Appellate Body in EC – Bananas III 252, reiterated that the Agreement on Agriculture's provisions on export subsidies for agricultural products were "specific provisions dealing specifically with the same matter" as the SCM Agreement prohibition on export subsidies. Thus, to apply the SCM Agreement to agricultural export subsidies would undermine the specificity of the agricultural regime, and the gradual process of reform which all Members had accepted. It would therefore be inconsistent with the object and purpose of the Agreement on Agriculture. This would nevertheless not render Article 13(c) meaningless because Article 13 in general, and Article 13(c) in particular, were intended to provide added clarity to the

249 Ibid., paras. 8.3-8.4.
250 US – FSC (Article 22.6 – US), Table A.1.
251 According to the European Communities, in the FSC dispute, the FSC scheme (and its successors) applied concurrently to exports of both agricultural goods and non-agricultural goods. For that reason, it made sense for the panel, and the EC as complainant, to argue that the two Agreements applied concurrently to the FSC scheme. In the present case; however, the CMO for sugar applied exclusively to agricultural products, and not to any non-agricultural products. In this case, the Complainants sought to apply the Agreement on Agriculture and the SCM Agreement not concurrently but cumulatively.
relationship between the two agreements during a specific time-period (the nine year implementation period for Article 13). Given the existence of Article 21.1 of the Agreement on Agriculture, the mere existence of Article 13(c) of the Agreement on Agriculture was not dispositive of a final conclusion on the relationship between the two agreements.

4.242 The Complainants submitted that the export subsidies granted in respect of exports of quota sugar, ACP/India equivalent sugar and C sugar were prohibited subsidies under Article 3.1(a) of the SCM Agreement. For the Complainants, the use of the term 'including' in Article 3.1 of the SCM Agreement made it clear that the items listed in the Illustrative List of Export Subsidies in Annex I of the SCM Agreement constituted subsidies contingent on export performance. Provided a measure fell within the definitional scope of any item in the Illustrative List, it would constitute a prohibited export subsidy for the purposes of Article 3.1 and 3.2 of the SCM Agreement. There was no need to determine whether a measure came within the definition of a subsidy for the purposes of Article 1.1 of that Agreement or to demonstrate export contingency, as the subsidy and contingency elements were inherent in the definitions. This had been confirmed by WTO jurisprudence.

4.243 The European Communities agreed with the Complainants but submitted that, nevertheless, the definition of "export subsidy" in Article 3.1 was still relevant context for interpreting the terms of the Illustrative List.

4.244 The Complainants argued that the European Communities' subsidies on C sugar exports were prohibited export subsidies within the meaning of Item (d) of the Illustrative List. (See full description of the Complainants' arguments in regard to Item (d) of the Illustrative List in Section IV.D.2(a)).

4.245 The Complainants also argued that Item (a) of the Illustrative List covered "[t]he provision by governments of direct subsidies to a firm or an industry contingent upon export performance." Since the European Communities' direct subsidies to sugar exporters upon the export of A and B quota as well as ACP/India equivalent sugar were contingent upon export, these subsidies were also prohibited through the operation of Item (a) of the Illustrative List and Articles 3.1(a) and 3.2 of the SCM Agreement.

4.246 In addition to its claims concerning Item (a) of the Illustrative List, Brazil argued that export subsidies granted by the European Communities on the sugar exported in excess of its reduction commitments were inconsistent with, and were prohibited by, Article 3 of the SCM Agreement. In this regard, Brazil referred to Article 1.1 of the SCM Agreement which defined a subsidy as a "financial contribution" that confers a benefit. For Brazil, exporters of A and B sugar and ACP/India "equivalent" sugar received at least two forms of financial contributions, each of which conferred a benefit within the meaning of Article 1.1 of the SCM Agreement. First, the payments received by exporters of A and B sugar and of ACP/India equivalent sugar constituted a "financial contribution" from the European Communities in the form of a direct transfer of funds, within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement.

4.247 Second, a financial contribution within the meaning of Article 1.1(a) of the SCM Agreement was also made if "there was any form of income or price support in the sense of Article XVI of GATT 1994". Article XVI:1 of GATT 1994 encompassed "any form of income or price support, which operates directly or indirectly to increase exports of any product from, or to reduce imports of any product into," the territory of a Member. The EC sugar regime did that. It increased exports of sugar from the European Communities by subsidizing the production of A and B quota sugar in excess of the amount consumed internally. These financial contributions conferred a benefit on their recipients within the meaning of Article 1.1(b) of the SCM Agreement because the recipients were, in the words of the Appellate Body, "better off" than they would otherwise have been."
4.248 Brazil also argued that the EC price support regime permitted producers to cover a disproportionate share of their fixed costs through guaranteed high returns on A and B quota beet and sugar, and also generated the production of C beet and C sugar. It was therefore a financial contribution to producers of C beet and C sugar within the meaning of Article 1.1 of the SCM Agreement. This financial contribution permitted them to produce and sell C beet and C sugar below the average total cost of production, thereby benefiting those producers. Since C sugar must be exported, and the C beet from which it was made was devoted exclusively to the production of C sugar, the subsidies received by the producers of C beet and C sugar were contingent on exports within the meaning of Article 3.1(a) of the SCM Agreement. These subsidies were, accordingly, prohibited by Articles 3.1(a) and 3.2 of the SCM Agreement.

4.249 The Complainants noted that if a panel were to find the measure at issue to be inconsistent with one of the multilateral trade agreements, such a finding normally would resolve the dispute. The panel could therefore refrain, on grounds of judicial economy, from making a finding that the measure was also inconsistent with another multilateral trade agreement. In the specific circumstances of this complaint, however, this was not the case.

4.250 The Complainants, referring to the text of Article 4.7 of the SCM Agreement, noted that the requirement to withdraw prohibited subsidies "without delay" had been interpreted by previous panels to mean that a Member must withdraw the subsidy at issue within 90 days from the date of the adoption of the panel report by the DSB. 253 They further noted that the Agreement on Agriculture did not have a similar provision aimed at the prompt withdrawal of subsidies in excess of reduction commitments. In the case of an inconsistency with that Agreement, only the substantially more lenient remedies set out in Articles 19 to 22 of the DSU applied. Nevertheless, Article 19.1 of the DSU did not serve to prevent a panel from making a recommendation in line with the provisions of Article 4.7 of the SCM Agreement, nor did Article 21.1 of the Agreement on Agriculture prevent a specific recommendation in line with Article 4.7 of the SCM Agreement.

4.251 According to Article 19 of the Agreement on Agriculture, the Complainants continued, the DSU applied to disputes under the Agreement on Agriculture. However, Article 1.2 of the DSU specified that special rules or procedures set out in the covered agreements and listed in Appendix 2 of the DSU "shall prevail" over the general dispute settlement rules and procedures set out in the DSU to the extent that "there is difference" between the rules and procedures. According to Appendix 2 of the DSU, Article 4.7 of the SCM Agreement was "a special or additional rule or procedure". Furthermore, it was one which entailed differences with the rules and procedures of Articles 19 to 21 of the DSU and consequently prevails over Article 19.1 of the DSU in disputes on prohibited subsidies. (see also paragraph 4.262 below)

4.252 A ruling under the SCM Agreement was, therefore, necessary to preserve the Complainants procedural right to a recommendation by the DSB that export subsidies prohibited under Agreement be withdrawn "without delay". If the Panel were to refrain from determining whether or not the measures at issue were prohibited under the SCM Agreement, the DSB would not be in the position to make such a decision. As a consequence, the Complainants would be deprived of their procedural right under Article 4.7 of the SCM Agreement. The Complainants noted that the Appellate Body decided in Australia-Salmon that panels should make the rulings necessary "to enable the DSB to make sufficiently precise recommendations and rulings so as to allow for prompt compliance" lest they engage in "false judicial economy". 254 For the Complainants, the Panel would be engaging in

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253 See for example, Panel Report on Canada – Aircraft Credits and Guarantees; Panel Report on Canada – Autos, para. 11.7; Panel Report on Canada – Aircraft, para. 10.4; Panel Report on Brazil – Aircraft, para. 8.5; and Panel Report on Australia – Automotive Leather II, para. 107.

false judicial economy if it were to refrain from making the substantive rulings necessary to enable the DSB to make a recommendation to which they are legally entitled.

4.253 The Complainants clarified that they had made a claim under the *SCM Agreement* because they believed that the European Communities was acting inconsistently with the provisions of that Agreement and that if the European Communities was found to be acting inconsistently, the remedy would follow. Thus, one of the reasons for invoking the *SCM Agreement* was to secure *all* of the rights to which the Complainants were entitled under *all* of the covered agreements that applied to the facts of this dispute. To the extent that these agreements provided different remedies, the Complainants were entitled to those different remedies.

4.254 The *European Communities* did not agree with the Complainants and, referring to the same statement made by the Appellate Body in *Australia – Salmon*, argued that panels were required to make rulings permitting the DSB to adopt sufficiently precise recommendations and rulings as to allow prompt compliance. To the extent that Article 4.7 of the *SCM Agreement* could be read as permitting partial withdrawal, and subsequent reinstatement of the same subsidy measure, then a ruling under the *SCM Agreement* would add nothing to the ability of the DSB to arrive at sufficiently precise and detailed rulings and recommendations to permit prompt and full compliance.

4.255 Referring to a previous WTO panel case in which export subsidies were found to be inconsistent with both the *SCM Agreement* and the *Agreement on Agriculture*, the Complainants noted that the panel in that case, at the request of the European Communities, recommended, pursuant to Article 4.7 of the *SCM Agreement*, that the DSB request the withdrawal of the subsidies without delay to the extent that they were inconsistent with the *SCM Agreement*. 255

4.256 Furthermore, *Thailand* submitted that the *Agreement on Agriculture* gave a limited and clearly delineated authorization to Members to provide subsidies in respect of agricultural products that would otherwise not be permitted. Citing Article 13(c)(ii) of the *Agreement on Agriculture*, Thailand contended that the logical implication of this provision was that, in respect of export subsidies that were inconsistent with the *Agreement on Agriculture*, the remedies set out in the *SCM Agreement* were available because it would otherwise not have been necessary to protect Members against challenges under the *SCM Agreement* during the implementation period. Thus, subsidization beyond the limits of that authorization, did not merit any protection from the remedies of the *SCM Agreement*. *Australia* and *Brazil* supported this approach.

4.257 The *European Communities* assumed that the existence of a specific remedy under Article 4.7 of the *SCM Agreement* was the main reason for the Complainants’ request for a ruling thereunder. The European Communities reiterated its position that the two agreements should not be applied cumulatively. In its view, the difficulty to reconcile the two sets of remedies was evidence of the fact that WTO negotiators never intended the agricultural export subsidy regime of the *Agreement on Agriculture* to apply cumulatively with the *SCM Agreement*. Under the *Agreement on Agriculture*, a Member had a limited authorisation to provide subsidies up to a specific ceiling, and an obligation not to provide other subsidies in a manner which could circumvent its commitments.

4.258 The European Communities argued that a finding that exports of C sugar and ACP/India equivalent sugar had been subsidized in excess of commitment levels would require the European Communities, in future years, to ensure that its total subsidized exports remained within its commitments. These would only be inconsistent with the *Agreement on Agriculture* if they exceeded the commitment levels. There would be no requirement, as such, that the European Communities remove subsidized exports of C sugar and the export refunds on ACP/India equivalent sugar.

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4.259 Thus, for the European Communities, while under the Agreement on Agriculture the measure providing the subsidy could be maintained (providing the relevant commitments were respected), under the SCM Agreement the measure providing the subsidy would have to be withdrawn without delay. This would mean that, if the commitments were exceeded at some point in a future year, the measure would have to be withdrawn, but that the losing Member would be able to reinstate it at the beginning of the next year. However, such a situation would clearly be ill-matched with the concept of withdrawal, which implied a permanent removal of a measure, and with the concept, in the second sentence of Article 4.7 of the SCM Agreement, that the measure should be withdrawn within a specific period of time. The European Communities referred to the findings of the panel in Canada – Dairy, which concluded256:

"In the Panel’s view, it results from Articles 8 and 21.1 of the Agreement on Agriculture and Article 3.1 of the SCM Agreement that the Panel would not be able to recommend Canada to ‘withdraw’ – as interpreted by the Appellate Body – measures constituting an export subsidy, exclusively in respect of agricultural products, both within the meaning of Article 9.1(c) of the Agreement on Agriculture and Article 3.1 of the SCM Agreement. Under Articles 3.3 and 8 of the Agreement on Agriculture, Canada has the right to provide export subsidies in respect of products specified in its Schedule, provided that it does not exceed the budgetary outlay and quantity commitment levels specified therein. Accordingly, if Canada has exceeded its quantity commitment levels, the Panel can only recommend Canada to bring its measures into conformity with its obligations under the Agreement on Agriculture."

4.260 The European Communities submitted that this reasoning was also applicable here.

4.261 The Complainants reiterated that the recommendations under Article 4.7 of the SCM Agreement differed from those under Article 19.1 of the DSU and referred to the observation of the Appellate Body in Brazil – Aircraft:

"Article 4.7 [of the SCM Agreement] contains several elements that are different from the provisions of Articles 19 to 21 of the DSU with respect to recommendations by a panel and implementation of rulings and recommendations of the DSB."

4.262 For the Complainants, there were essentially three differences between the remedy, and the implementation of recommendations and rulings, provided by Articles 19 to 21 of the DSU and that provided by Article 4.7 of the SCM Agreement:

- **Nature of the remedy:** Under Article 19.1 of the DSU, the Panel shall recommend that the measure at issue be brought into conformity while Article 4.7 of the SCM Agreement required the recommendation that the prohibited subsidy be withdrawn.

- **Timeframe:** According to Article 21.3 of the DSU, the measure at issue shall be brought into conformity within "a reasonable period of time" while Article 4.7 of the SCM Agreement required the recommendation that the prohibited subsidy be withdrawn "without delay".

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257 Appellate Body Report on Brazil – Aircraft, para. 191. See also Panel Report on Australia – Automotive Leather II (Article 21.5 – US), paras. 6.41 and 6.42, where the panel held that "’[w]ithdraw the subsidy’ [in Article 4.7] is … different from ‘bring the measure into conformity’, the recommendation required under Article 19.1 of the DSU’, and therefore that ‘to the extent that ‘withdraw the subsidy’ requires some action that was different from ‘bring the measure into conformity’, it was that different action which prevails”
• **Procedures:** According to Article 21.3(c) of the DSU, the implementation period shall be determined by binding arbitration, while Article 4.7 of the SCM Agreement assigned the task of determining the implementation period to the panel.

4.263 Of the three differences listed above, the third was of particular importance to the Complainants in order to avoid further negotiations with the European Communities and possibly a lengthy and complex arbitration procedure to resolve a matter that could and should be resolved by this Panel.

4.264 **Thailand** recognized that the European Communities was entitled to grant export subsidies in respect of sugar within the limits of its export reduction commitments and that, consequently, the Panel could not recommend that the DSB request the European Communities to withdraw *all* of its export subsidies on sugar. In *Canada – Dairy (Article 21.5 – New Zealand and US)*, the panel correctly found that such a recommendation could not be reconciled with Article 21 of the *Agreement on Agriculture*, according to which the provisions of the *SCM Agreement* applied subject to those of the *Agreement on Agriculture*. In its first submission, Thailand therefore specifically requested the Panel to recommend that the DSB request the European Communities to bring its export subsidies for sugar into conformity with its obligations under the *Agreement on Agriculture* by withdrawing the export subsidies for sugar that were inconsistent with the *Agreement on Agriculture*. Thailand thus requested the recommendation according to Article 4.7 of the *SCM Agreement* only in respect of the subsidization that exceeded the European Communities’ rights under the *Agreement on Agriculture*. Thailand’s request was therefore fully consistent with the principle set out in Article 21 of the *Agreement on Agriculture*.

4.265 **Brazil** considered that the Panel should find an inconsistency with both agreements and recommend both remedies. It could do the latter by recommending that the Member concerned bring its measure into compliance by withdrawing the prohibited subsidy without delay. In this regard, Brazil noted that the purpose of the export subsidy provisions of the *Agreement on Agriculture* was to provide a "safe harbour" for those subsidies that complied with the reduction commitment obligations of the Agreement; it was not to deny Members the remedies to which they were entitled under the *SCM Agreement* for export subsidies that did not comply with the requirements of the *Agreement on Agriculture*. **Australia** concurred with this approach and recalled that, in the original *US-FSC* case, the DSB recommended that the United States bring the FSC measure into conformity with its obligations under the covered agreements and that the FSC subsidies found to be prohibited export subsidies within the meaning of the *SCM Agreement* be withdrawn without delay.

4.266 The **European Communities** responded that the application of Article 4.7 of the *SCM Agreement* would amount to denying the European Communities’ right to maintain export subsidies up to the commitment levels specified in its Schedule and that this was inconsistent with Article 21.1 of the *Agreement on Agriculture* which provided that other Annex 1A Agreements only applied subject to the *Agreement on Agriculture*; in other words, the application of the other Agreements could not nullify the rights of WTO Members under the *Agreement on Agriculture*.

G. **Nullification or Impairment**

4.267 Subsidiarily, the **European Communities** contended that the claim submitted by the Complainants with respect to the C-sugar regime involved a complaint of the so-called "violation" type described in Article XXIII.1(b) of the GATT 1994, which referred to the situation where a Member considered that a "benefit accruing to it directly or indirectly is being nullified or impaired … as the result of … the failure of another contracting party to carry out its obligations under this

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Citing Article 3.8 of the DSU, the European Communities submitted that Article 3.8 of the DSU made clear that, while a finding of violation of a covered agreement gave rise to a presumption of nullification or impairment of benefits accruing under that agreement, the defending party had the possibility to rebut such a presumption.

4.268 The European Communities held that, even if the C sugar regime resulted in a violation of Articles 3.3, 8 or 10.1 of the Agreement on Agriculture, such violation would not nullify or impair any benefits accruing to the complaining parties under those provisions as the Complainants could have had no reasonable expectations that the European Communities would take any measure to reduce its exports of C sugar. Those Articles did not confer a right to a certain volume or amount of trade, the European Communities continued. Rather, the "benefits" accruing under Articles 3.3, 8 and 10 of the Agreement on Agriculture consisted of the expectations of improved competitive opportunities which arose out of the limitations placed on export subsidies by those provisions.

4.269 The European Communities referred in particular to the Appellate Body report in India – Patent (US) in which case the Appellate Body emphasized that the expectations of the complaining party only become relevant after a violation had been found, as part of the examination of whether such violation led to nullification or impairment. At the time of the conclusion of the WTO Agreement, the European Communities continued, and until recently, the Complainants had shared the European Communities' understanding that the C sugar regime did not provide export subsidies and, therefore, could have had no expectations that the European Communities would reduce its exports of C sugar. The European Communities considered, therefore, that the Complainants could not now act as if their expectations were being nullified or impaired by the alleged inconsistency with Articles 3, 8 or 10.1 of the Agreement on Agriculture.

4.270 The European Communities submitted that, if nevertheless the Panel were of the view that the Complainants were entitled to expect that the European Communities would reduce its exports of C sugar such expectations would be limited to a 21 per cent reduction, as envisaged in the Modalities Paper with respect to all export subsidies, rather than their complete elimination. Accordingly, the alleged violation of Articles 3, 8 and 10.1 of the Agreement on Agriculture would nullify or impair benefits accruing to the Complainants only to the extent that the current volume of subsidized exports exceeded 79 per cent of the quantity of subsidized exports made during the base period.

4.271 Moreover, for the same reasons as for C sugar, the European Communities contended, the alleged violation in respect of ACP/India equivalent sugar did not nullify or impair any benefits accruing to the Complainants, because they could have had no expectations that the European Communities would reduce the quantity of subsidized exports mentioned therein (see also paragraph 4.283).

4.272 Australia submitted that the European Communities' infringement of its obligations under the Agreement on Agriculture and the SCM Agreement had resulted in a prima facie case that nullification and impairment had been suffered by Australia. Australia recalled that, pursuant to Article 3.8 of the DSU, the European Communities, as the defending party, had to rebut the presumption of nullification and impairment.

4.273 Australia considered that the assertion by the European Communities that the Complainants could have had no expectations of improved competitive opportunities in relation to C sugar and ACP/India equivalent sugar and that, therefore, no benefits had been nullified or impaired, was a

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259 Articles XXII and XXIII of the GATT apply to dispute settlements under the Agreement on Agriculture pursuant to Article 19 of the latter Agreement.


261 See in particular Section III.5 of the European Communities' first written submission.
novel argument. Australia contended that this argument did not counter the presumption in Article 3.8 of the DSU which required the European Communities to establish that its breach of its WTO obligations has had no "adverse impact" on Australia.

4.274 Referring to the Appellate Body report in EC – Bananas III and its reference to the US – Superfund case with respect to its discussion of the rebuttal of nullification or impairment, as well as to the panel report in Turkey – Textiles on the same subject, Australia submitted that the European Communities had not provided any evidence in this case, to rebut the presumption of nullification and impairment. The mere fact that the Complainants might have increased exports was irrelevant to the determination of this issue.

4.275 Contrary to the European Communities' assertions, Australia continued, the relevant provisions of the Agreement on Agriculture and the SCM Agreement did not merely serve to confer legitimate expectations in regard to a certain volume of reductions. The Agreement on Agriculture conferred a right to expect that the European Communities would act in conformity with its obligations, including that the European Communities would subject its export subsidies to reduction commitments, that it would not provide export subsidies in excess of scheduled commitments and that it would not circumvent those commitments. The SCM Agreement conferred upon Australia a right that the European Communities would not grant or maintain export subsidies on sugar except as provided in the Agreement on Agriculture.

4.276 Responding to the European Communities' arguments in paragraph 4.268-4.269 above, Brazil submitted that Article 3.8 of the DSU specified that a violation was prima facie evidence of nullification or impairment. The European Communities had introduced no evidence to rebut that presumption. Moreover, the European Communities' reliance on the Appellate Body's opinion in India – Patent (US) was, according to Brazil, misplaced as that case involved reliance on expectations to establish a violation. In this case, it was the violation that nullified or impaired the Complainants' legitimate expectations. The Complainants' legitimate expectations of improvement in the competitive relationship of their sugar and that exported by the European Communities were nullified or impaired when their sugar competed in the world market with EC sugar that was exported, with the aid of subsidies, in excess of the European Communities' reduction commitments.

4.277 As concerns the footnote, Brazil submitted that the points discussed in connection with C sugar also applied, mutatis mutandis to ACP/India equivalent sugar.

4.278 Thailand contended that the European Communities was putting forward a novel legal theory according to which a WTO-inconsistent measure did not nullify or impair benefits accruing under a covered agreement if it could be expected. Thailand submitted that Article 3.8 of the DSU defined clearly what the European Communities must establish to rebut the presumption of nullification and impairment: it must demonstrate that its breach of the rules had not had "an adverse impact" on Thailand. Thailand considered that the European Communities had not done so.

4.279 The European Communities replied that even if exports of C sugar were found to benefit from export subsidies and were in excess of the European Communities' reduction commitments and even if the Complainants were not barred from bringing a claim to that effect by Article 3.10 of the DSU and the principle of good faith, the alleged violation would not, in any event, nullify or impair any benefits accruing to the Complainants.

263 Panel Report on Turkey – Textiles, para. 9.204.
264 European Communities' first written submission, para. 147.
4.280 Referring to Brazil's arguments in paragraph 4.276 above, the European Communities explained that it relied on India – Patent (US) for the proposition that in this case the existence of nullification or impairment should be assessed by looking at the legitimate expectations of the Complainants. The European Communities submitted that the Brazilian arguments overlooked the thrust of the European Communities' defence, which was precisely that Brazil could have no "legitimate expectations" that the European Communities would stop its exports of C sugar. At most, Brazil could have expected that the European Communities would reduce those exports by 21 per cent (in quantity) as agreed in the Modalities Paper.

4.281 Responding to Thailand's arguments in paragraph 4.278 above, the European Communities submitted that it had shown that Thailand had suffered no "adverse impact" because the Complainants had no expectations that the European Communities would stop exporting C sugar. The European Communities considered that the relevance of expectations in establishing the existence of nullification or impairment was not a "novel legal theory". It was confirmed by the case law cited in the European Communities' first written submission, which Thailand did not address. The European Communities disagreed that it had to show that the alleged violation had had no actual effect on Thailand's exports in order to establish the absence of an "adverse impact". In the opinion of the European Communities, that was not required by the ordinary meaning of the term "adverse impact".

4.282 If the European Communities were to reduce its exports of sugar by 60 per cent, as requested by the Complainants, it would be doing much more than removing any "adverse impact" suffered by them. It would be providing the Complainants with an advantage that none of them expected, nor could have expected, at the conclusion of the Uruguay Round. The ultimate purpose of dispute settlement procedures, the European Communities observed, was to maintain the agreed balance of concessions and not to present some Members with a windfall profit at the expense of another Member. The notion of "nullification and impairment" must be interpreted in the light of that purpose.

4.283 Finally, for the reasons explained in its various submissions with respect to C sugar, the European Communities recalled that, subsidiarily, in the same sense as there had been no nullification and impairment in respect of C sugar, there had been no such nullification and impairment in respect of ACP/India equivalent sugar.

4.284 Brazil recalled, in response to arguments to the effect that the Complainants' claims would lead to serious harm to some developing countries, that two of the Complainants, Brazil and Thailand, were themselves developing countries whose benefits were most certainly being nullified or impaired. Brazil also recalled the European Communities' arguments that nothing in its sugar regime nullified or impaired any benefits accruing to Complainants under the Agreement on Agriculture. Referring to a March 2004 study by Oxfam which had calculated, based on 2002 exports, that the EC sugar regime caused immediate losses of $494 million for Brazil and $151 million for Thailand in that year alone, Brazil submitted that that was serious nullification or impairment by any reasonable standard. Brazil and Thailand were not the only developing countries hurt by the European Communities' sugar regime. Oxfam noted the cost to South Africa and a number of other developing countries, and the Panel had heard directly from Colombia and Paraguay concerning the harm the regime did to them.

265 Thailand's oral statement, first substantive meeting, para. 44.
266 Exhibit ALA-12.
V. ARGUMENTS BY THIRD PARTIES

5.1 The ACP countries explained that the objectives of the EC/ACP Partnership Agreement had been in the centre of the EC-ACP relationships since the beginning. These objectives underpinned all the preferential agreements, including the Sugar Protocol, and had always been in line with GATT and WTO objectives for positive and effective efforts towards the sustainable development of developing and least developed countries. They submitted that they had substantial trade interests and systemic interests in the present dispute in ensuring the proper interpretation and application of the WTO Agreement on Agriculture so as not to destabilize the balance of concessions reached at the end of the Uruguay Round and which concerned all Members, including the ACP and the Complainants. They were of the opinion that the upholding of the claims of the complainants would have serious adverse consequences on the trade and economic benefits, which they currently derived from the export of sugar to the European Communities under the ACP/EC trading arrangement on sugar (Sugar Protocol).

5.2 Exports to the EC market constituted a vital outlet for the ACP sugar supplying states. They noted that they benefited from guaranteed preferential access to the EC market and remunerative prices for their exports. The obligations of the European Communities in respect of the Sugar Protocol had to be fulfilled within the framework of the EC sugar regime and the European Communities was importing fixed quantities of raw cane sugar, from the ACP countries, at guaranteed prices equivalent to the EC intervention prices.

5.3 This guaranteed level of prices, they asserted, ensured predictable and stable earnings crucial for the economic and social development of these developing and least developed countries, for whose economies sugar represented their life-blood. The Sugar Protocol had been a key factor in the socio-economic development of the ACP countries, enabling them to meet, to a certain extent, the objectives set out in the Preamble of the Marrakech Agreement, namely raising the standards of living, ensuring full employment and a steady volume of real income. The ACP sugar industries played a multifunctional role in their respective economies. More specifically, they promoted rural development, poverty alleviation, social development, social peace, protection of the environment as well as the tourism industry.

5.4 The ACP countries explained that during the period 1999-2001, exports under the Sugar Protocol accounted, on average, for 50.6 per cent of agricultural exports and 13.6 per cent of GDP of the ACP countries concerned. During the same period, the number of persons employed in the sugar sector was on average 43.8 per cent of the total number of persons employed in agriculture. These figures had to be compared with the very small share of the sugar market of the ACP in terms of world trade: the 1.6 million tonnes exported to the European Communities represented 3.6 per cent of world trade in sugar. This trade corresponded to 0.18 per cent of global agricultural trade. While these exports had, they contended, a minute effect on global trade, the same exports were critical to the economic growth of the ACP countries which included least-developed, net-food importing, landlocked or island states and single-commodity producers/exporters with specific economic and social difficulties.

267 Barbados, Belize, Fiji, Guyana, Côte d’Ivoire, Jamaica, Kenya, Madagascar, Malawi, Mauritius, St. Kitts & Nevis, Swaziland, Tanzania and Trinidad & Tobago presented a joint written submission as well as a joint oral presentation as ACP Sugar Supplying States (ACP countries). Each of these countries also separately endorsed the views expressed in paras. 5.1-5.12. The distinctive arguments elaborated by each of these countries presented separately in their own written submissions or oral statements have been briefly reflected individually.

268 ACP countries benefiting from the Sugar Protocol.
5.5 The preferences granted to the ACP sugar exporting countries in terms of market access and the scope of the reduction commitments of the European Communities in the Uruguay Round, the ACP countries submitted, were to be considered as a whole and not in isolation from the European Communities' export possibilities. The purpose of Footnote 1 in the EC Schedule, interpreted in the context of both the Sugar Protocol and the CMO, was, in the opinion of the ACP countries, to allow for the exportation by the European Communities of quantities corresponding to those imported under the preferential agreements. The ACP countries were of the view that the Complainants' claim that the European Communities was not complying with the terms of the footnote, did not fall within the terms of reference of the Panel. However, should the Panel decide that there were grounds for examining this claim, an interpretation in good faith, based on the rules of interpretation applying in the context of the WTO, i.e. Articles 31(1), 31(4) and, if needed, 32 of the Vienna Convention, allowed no other reading than what was well known to the Complainants prior to and during the negotiations, i.e. that the European Communities intended to keep the possibility to grant export refunds on exports of a quantity corresponding to the quantities imported under the preferential agreements concluded with the ACP countries and India. This was a fundamental element of the balance achieved within the EC sugar regime. Therefore, the footnote to the EC's Schedule must, and could only be interpreted to cover corresponding exports, based on the ordinary meaning of its terms and the necessity to give an *effet utile* to its wording.

5.6 With respect to the interpretation of the footnote, the ACP countries argued that, applying Article 31(1) of the Vienna Convention\(^\text{269}\), the footnote should be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its objects and purpose. Accordingly, they claimed that, as regards the "terms" of the footnote, based on the necessity to give an *effet utile* to its wording, "exports of sugar of ACP and Indian origin" could not mean anything else but exports of white sugar in quantities corresponding to the quantities of raw cane sugar imported under the EC/ACP and EC/India preferential arrangements. This would be, they argued, the only interpretation providing the footnote with an operative meaning, and which would truly reflect the intention of all the parties.\(^\text{270}\) Furthermore, the ACP countries asserted that the Sugar Protocol as well as the EC Regulation on the CMO would allow a proper understanding of not only the context of the footnote, but also its necessity, and therefore its object and purpose.\(^\text{271}\) In this sense, the ACP countries concluded that the footnote must be interpreted so as to allow the European Communities to export 1.6 million tons of white sugar, corresponding to its imports of ACP/Indian raw sugar, with the benefit of export refunds.

5.7 With respect to the Agreement on Agriculture, the ACP countries were of the view that it primarily defined exports subsidies commitments as a limitation. Accordingly, WTO Members would enjoy a certain flexibility. Referring to the text of Article 3.1 of the Agreement on Agriculture, they argued that in *Canada – Dairy*, the Appellate Body acknowledged the importance of the limitation concept by describing an export subsidy commitment as "an undertaking to limit the quantity of exports that may be subsidized.\(^\text{272}\) The European Communities was therefore entitled to maintain an export subsidy on an agricultural product within the limits of its commitments.

5.8 Referring to the Appellate Body report in *Korea – Various Measures on Beef*\(^\text{273}\), the ACP countries contended that, when taken together, the two components of the European Communities' export subsidy commitments indicated that the total amount of export refunds granted on exports of sugar, as a whole, had been declining. Accordingly, the specific structure of the European Communities' commitments had been working, *de facto*, as a limitation of the level of subsidies.

\(^\text{269}\) ACP written submission, para. 78.
\(^\text{270}\) Ibid., paras. 89-93.
\(^\text{271}\) Ibid., para. 95.
granted on its exports of sugar. Therefore, in the opinion of the ACP countries, the European Communities had complied with its export subsidy commitments.

5.9 With respect to the US – Sugar Waiver and the EC – Bananas III cases referred to by the Complainants, the ACP countries asserted that the issue at stake and the very nature of the legal provisions under consideration in this case were different. The set of provisions referred to by the Complainants, i.e. Articles 3, 8 and 9 of the Agreement on Agriculture did not provide for such a general prohibition but rather for a limited authorization for Members to provide subsidies up to the level of the reduction commitments specified in their Schedule. In addition, in the case of export subsidy commitments, the benefits that WTO Members could expect were based on the improvement of the competitive environment resulting from the reduction of subsidization undertaken in conformity with the commitments and were of a different nature from those resulting from market access commitments. The Complainants could not have had any reasonable expectation that the European Communities would reduce the quantities mentioned in the footnote. As a result, no specific benefits could have been impaired or nullified by the European Communities’ exports of 1.6 million tons with the benefit of export refunds.

5.10 Referring to "estoppel" as "a general principle of international law deriving from the broader principle of good faith", the ACP countries submitted that the Complainants were precluded from bringing a claim against the validity of the footnote since they had acquiesced to the insertion of the footnote in the European Communities’ Schedule of Commitments and had given assurances of this acceptance by not raising any formal claims to that effect since the conclusion of the Uruguay Round. The interests not only of the European Communities, but also of the ACP countries, would be substantially prejudiced if the Complainants were allowed to challenge what they previously acquiesced to. Indeed, should the Panel accept the claims of the Complainants, it would mean that the Panel would allow them to benefit, de facto, from a reduction of 60 per cent of the quantities on which the European Communities was entitled to grant export refunds.

5.11 The ACP countries referred to the relevance of the EC – Computer Equipment case in particular regarding, firstly, the fact that all the schedules of Members represented a common agreement among all Members, and, secondly, the obligations of all participants in respect of verification.

5.12 The ACP countries endorsed the European Communities’ position with respect to the C sugar issue and the SCM Agreement issue.

5.13 Barbados added that to understand the full implications of what the likely consequences of a decision unfavourable to the European Communities could mean to the ACP countries, it would be important to consider the characteristics of the sugar industry within these countries and the critical role sugar played in their development.

5.14 Barbados noted that it was not a major agricultural producer but the sugar industry, which was more than 300 years old, had maintained its dominant position within its small agricultural sector. Sugar was still the largest single agricultural export crop and earned the most foreign exchange in that sector. Consequently, agriculture generally, and sugar in particular, continued to play a strategic role as Barbados endeavoured to restructure its economy in the face of the challenges resulting from liberalization and globalization. The economic and social benefits derived from the production and export of sugar were evident in a number of areas, including contribution to the gross domestic product (“GDP”), employment, foreign exchange earnings and food security. The sugar industry accounted for an average of 40 per cent of the agricultural sector’s input to real GDP in the period 1998 to 2002. For the same period, direct employment in the industry averaged 1200 persons, while

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274 See also ACP statement in paras. 5.1-5.12 above.
indirect employment was significantly higher. The export of bulk raw sugar earned Barbados an average of US $25 million per year during the same 5-year span.

5.15 Barbados explained that as a small, vulnerable Net Food-Importing Developing Country (NFIDC) which already imported approximately 75 per cent of its food, food security was a major concern. Sugar cane was one of the few crops appropriate for large-scale cultivation under the climatic and agronomic conditions in Barbados and could be fairly regarded as a stabilising factor within the agricultural sector. The sugar industry therefore played a major role in helping Barbados achieve its food security goals by maintaining a significant area of the island's landmass under agricultural production with a systematic crop rotation process and also by providing a vital source of foreign revenue.

5.16 Barbados contended that the foreign exchange earnings from the sugar exports would be significantly lower without the preferential margin enjoyed under the ACP/EC Sugar Protocol. Barbados was therefore deeply concerned about the current dispute and the potentially negative impact that an adverse decision of this Panel was likely to have on the EC price for ACP sugar.  

5.17 Belize submitted that the multilateral rules-based trading system would only be sustained if innovative mechanisms existed to provide all Members, even the most vulnerable, with a share in the growth in international trade commensurate with the needs of their economic development. Belize was generally categorized as a mono-crop society. It was an import-oriented economy, dependent on the exports of a few traditional commodities to generate its revenue: approximately 20 per cent of the country's population was dependent on the sugar trade. Given its high cost of production of consumer goods and its small population, it was unable to produce most of what it consumed. Further erosion of its ability to pay for imports would have severe consequences; 33 per cent of the population already lived below the poverty line. It noted that it contributed less than one per cent to total world sugar exports, but alterations to the present EC sugar regime could severely impact the fundamental fabric of the Belizean society.

5.18 Belize submitted further that a disruption of the pricing mechanism would have an adverse impact on the preferential arrangements covered by the Sugar Protocol. It argued that the various components of the EC sugar regime depended upon each other in so systemic a manner that the utmost care should be taken in attempting to rearrange its mechanism. To dismantle any particular aspect of the regime would tend to weaken and damage the very fabric of the preferential agreement: its quota system, its price structure, and its system of compensation. Accordingly, Belize held that the possible impact of each proposed change should be taken into account in assessing its overall implications on the world's trading system.

5.19 Belize was of the view that the footnote fully concurred with the obligations of the European Communities, expressing the Members' agreement with respect to what was an appropriate provision addressing the circumstances of vulnerable small developing countries within the broad rules-based framework. Belize also considered that the EC sugar regime, including the exports of refined sugar with the benefit of export refunds, was an integral part of the EC sugar regime and, as such, contributed to its overall balance and stability.

5.20 Canada submitted that Article 9.1(c) must be read so as to maintain the distinction between domestic support and export subsidies. With respect to the three distinct elements of Article 9.1(c), "payment", "on the export" and "financed by virtue of government action", Canada noted that only the

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275 Third party oral statement by Barbados.
276 See also ACP statement in paras. 5.1-5.12 above.
278 Third party oral statement by Belize.
first and third of these elements were at issue before the Appellate Body in Canada – Dairy. Therefore, that analysis could not be applied automatically in the present dispute. Canada was of the view that the Panel should turn to a contextual reading of Article 9.1(c), looking at the whole of the Article and its place in the Agreement on Agriculture, to provide guidance as to the appropriate relationship between these elements.

5.21 Canada expressed concern over the suggestion that the average cost of production would be the only appropriate benchmark against which to measure "payments". In the light of the Canada – Dairy decisions and the variety of transactions identified by the Complainants, Canada requested clarification with respect to the systemic meaning of "payments". Furthermore, Canada stressed the importance of ensuring that context-specific benchmarks or guidelines used in previous disputes were not confused with legal standards derived directly from the text of the Agreement on Agriculture.

5.22 With respect to Article 3.1(a) of the SCM Agreement, Canada recalled, the Appellate Body had held that contingency did not suggest a simple relationship of payment and export. Rather, the grant of a subsidy must be conditional or dependent upon export performance; it must be "tied to" export performance. Referring to the common interpretation of "export contingent" as found by the Appellate Body in US – FSC and Canada – Aircraft (Article 21.5 – Brazil), Canada was of the opinion that an indirect benefit, i.e., a cross-subsidy, that could result in an unintended or consequential export, did not lead to a finding that an export subsidy was provided pursuant to Article 9.1(c). Finally, Canada noted that despite it being true that sugar production in the European Communities was the subject of a complex regulatory regime; this complexity was not by itself proof that C sugar benefited from export subsidies.

5.23 Canada also requested clarification with respect to the relation between the various programmes, measures and transfers alleged by the Complainants to result in export subsidies, and the governmental actions that ostensibly finance those subsidies, i.e. if such financing could occur as a result of cross-subsidization, where was the threshold between actions that resulted in cross-subsidization and actions that did not?

5.24 Canada recalled that the Appellate Body had explained that the words "by virtue of" defined the relationship between governmental action and the financing of payments under Article 9.1(c). That relationship was the link between a given action and the financing of payments "on the export". Canada asserted that this link did not exist merely by virtue of government measures that permitted payments to occur; instead, the words "by virtue of" demanded a demonstrable link between the governmental action and the payments allegedly financed by that action.

5.25 China submitted, with respect to the question of burden of proof under Article 10.3 of the Agreement on Agriculture, that the European Communities must establish the "export subsidization aspect" with respect to claims of violation of Articles 3, 8, 9 and 10 and the consequences of any doubts about the European Communities' evidence of export subsidization should be borne by the European Communities. The European Communities should therefore fulfil its burden by submitting evidence sufficient to establish that the disputed measure did not represent an export subsidy, or benefits were not granted with respect to a quantity of the product in question in excess of its reduction commitment level, or both. As concerns Article 3.3 of the Agreement on Agriculture, China

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280 Third party written submission of Canada, para. 10.
281 Ibid., paras. 16-18.
282 Ibid., para. 7.
286 Third party written submission, para. 28, and oral statement of Canada.
considered that it did not allow any WTO Member to derogate from the export subsidy commitments contemplated therein. China recalled the Appellate Body report in US-FSC which explained that both scheduled and unscheduled agricultural products were subject to export subsidy commitments. With respect to "scheduled" products, a Member was entitled to provide export subsidies within the "limited authorization", which specifically referred to the "budgetary outlay and quantity commitment levels" specified in that Member's Schedule. China contended that sugar fell within the product coverage under Article 2 and Annex 1 to the Agreement on Agriculture, and had been "scheduled" in the "Description of products" of the EC's Schedule. Since "C sugar" was neither beyond the product coverage of the Agreement on Agriculture, nor a separate categorised product description of the Schedule. Thus, it should be logically deemed as being incorporated into the Schedule and subject to reduction commitments under Article 3.3 of the Agreement on Agriculture. Should the European Communities consider C sugar as a product other than a "scheduled" agricultural product, it should as a consequence be subject to the "prohibition" against provision of export subsidies on "unscheduled" agricultural products.

5.26 With respect to the role of the Modalities Paper as a relevant element of the historical context within the meaning of Article 31.1(b) of the Vienna Convention, China recalled that the note by the chairman of the Market Access Group explicitly precluded the use of the negotiating modalities as a basis for dispute settlement proceedings under the "MTO" Agreement. Furthermore, China noted that the Appellate Body in EC – Bananas III observed that the Agreement on Agriculture made no reference to the Modalities document or to any 'common understanding' among the negotiators of the Agreement on Agriculture.

5.27 As concerns the notion of the "average total cost of production", China saw no reason why this should not be adopted as the benchmark or objective standard, for the determination of whether the exports of C sugar involved "payments" under Article 9.1(c) of the Agreement on Agriculture. Furthermore, recalling the Appellate Body report in Canada – Dairy (Article 21.5 – New Zealand and US II), China considered that since the higher revenue sales in the EC sugar market effectively financed part of the lower revenue sales on world markets, "by funding the portion of the shared fixed costs" of production "attributable to the lower priced products", i.e. C sugar, the demonstrable link between the EC governmental action and the "financing" was well established. The identification of the "average total costs of production" must be illustrated and objective, by taking into account any marginal costs of the EC sugar production on an industry-wide basis.

5.28 Referring to the interpretation of the footnote in the EC's Schedule, China recalled that the European Communities had explained, before the WTO Committee on Agriculture, that:

"[A]s indicated in footnote 1 of the table on export subsidies contained in Part IV, Section II of Schedule CXL, the EC is not undertaking any reduction commitment on exports of ACP or Indian sugar. Consequently, any financial assistance is not reported to the WTO. For information, these exports amount to approximately 1.6 million tonnes per year." (emphasis added)

5.29 China submitted that the footnote at issue was intended to exempt the European Communities from "undertaking" any reduction commitment with respect to "any financial assistance" and

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287 Modalities for the establishment of specific binding commitments under the reform programme – Note by the Chairman of the Market Access Group, MTN.GNG/MA/W/24, 20 December 1993.
288 Appellate Body Report on EC – Bananas III.
289 Ibid., para. 98.
290 Ibid., para. 45.
291 Committee on Agriculture, summary report of the meeting held on 17-18 November 1998 (G/AG/R/17, 25 January 1999) p. 29. See also first submission of Thailand, para.95.
notification requirements on exports amounting to approximately 1.6 million tonnes per year of
"ACP/Indian origin" sugar. China was of the view that the European Communities must demonstrate
or establish the legal basis for the exemption of "ACP/India equivalent sugar" from reduction
commitments. Due to the equivocal meanings derived from the footnote, the European Communities'
"two – parts" interpretation of its subsidy commitments – i.e. "limits" subject to reduction in respect
of "scheduled" sugar and "a fixed ceiling" in respect of "ACP/India equivalent sugar" – could not, in
China's opinion, be justified as representing "a common agreement among all Members".  

5.30 Colombia noted that it was the eighth largest exporter of sugar in the world and had one of
the lowest cost of production levels and highest yields per hectare. Considering that Colombia could
count on an efficient and productive sector, Colombia was facing many difficulties participating in
international trade, not only in the European Communities but also in other countries. The distortions
in the price of sugar, in particular those which resulted from the complex regulation of the European
market, were causing problems to the Colombian exports not only in the Europe but also in other
markets in which those distortions had been identified as the reason for Colombia's limited access.
Therefore, this dispute had both a systemic and commercial importance to Colombia.

5.31 Referring to the legal value of the footnote, Colombia enquired whether there was a legal
basis to exclude a quantity of sugar equivalent to the European Communities' imports from India and
ACP countries from the export subsidies reduction commitments. Colombia was of the view that,
since exceptions in the WTO must be agreed upon through the multilateral procedure provided in
Article IX of the Marrakech Agreement, the possibility of granting legal value to the footnote would
be unrealistic.

5.32 With regard to the concept of estoppel, Colombia noted that it had never been recognised in
the jurisprudence of the WTO and the concept in itself had its application limited to bilateral
relationships. Accordingly, even if the Panel found that some Members were aware of the European
Communities' exemption to the reduction commitments, it was unthinkable that such a "bilateral
understanding" could be applied in the multilateral context.

5.33 Colombia considered that there were two types of export subsidy commitment. The first
related to reduction and prohibition as laid down in Articles 8 and 9 of the Agreement on Agriculture.
The combination of agreed disciplines under those Articles implied, according to Colombia, that
subsidies included by Members in their Schedules must be reduced in accordance with multilateral
disciplines. Similarly, in its interpretation, subsidies for which no phasing-out commitments had been
made should be prohibited.

5.34 The second export subsidy commitment, Colombia continued, related to anti-circumvention
and was governed by Article 10.1 of the Agreement on Agriculture. Colombia was of the view that
Article 10.1 applied only to expressly permitted subsidies. Its objective was to discipline the manner
in which those subsidies were applied in order to avoid that such application resulted in, or threatened
to lead to, circumvention of export subsidy commitments.  

5.35 Côte d'Ivoire submitted that, by contesting the EC sugar regime, the Complainants put into
question the basis for cooperation between Côte d'Ivoire and the European Communities. If
successful, the Complainants allegations would have serious socio-economic consequences for the
country. Côte d'Ivoire explained that the sugar industry was highly important to the economy of the
country. It started as a bold government policy in the 1970s to diversify agriculture production and
thus create a regional development pole in the north of the country. In the last few years, the sugar

292 Third party written submission and oral statement by China.
293 Third party oral statement by Colombia.
294 See also ACP statement in paras. 5.1-5.12 above.
industry had experienced a clear development as Côte d'Ivoire privatized its sugar industry in 1997. Today, the industry was represented by two companies, Sucaf-Ci and Sucréivoire with sugar production being the second most important activity after cotton in the north of Côte d'Ivoire.

5.36 In the last five years, €85 million had been invested in order to increase the country's sugar production, which thus went from 120,000 tonnes in 1997 to 170,000 tonnes currently, exceeding local consumption by some 20,000 tonnes per year. Most of this quantity was exported to the European Communities under the Sugar Protocol and the SPS arrangements, representing some 15 per cent of the sugar revenues of Côte d'Ivoire.

5.37 The sugar industry, Côte d'Ivoire continued, employed some 2,000 individuals directly and another 5,000 indirectly which, in the African context represented revenues for the subsistence of around 200,000 people. On top of the approximately 22,000 hectares industrially planted, some 2,400 hectares were village plantations, a policy recommended by the government and which had led to the reinsertion of some 800 families.

5.38 In conclusion, Côte d'Ivoire, not wishing to see the only efficient international co-operation arrangement destroyed, hoped that the Panel would contribute to put development as an essential objective at the heart of the discussions.  

5.39 Cuba noted that sugar was one of its chief export items but Cuba was also interested in averting the erosion of the tariff preferences granted to the ACP States under the EC sugar regime. Cuba considered that this dispute must be viewed in the light of the basic objectives of the GATT 1994, which included raising standards of living and securing the progressive development of economies, while paying special attention to the fact that the achievement of these objectives was "particularly urgent" for the least-developed economies.

5.40 Export income, Cuba continued, played a crucial role in many underdeveloped economies as their main source of subsistence and an important factor of economic development. The size of that income depended on the prices countries paid for essential imported products, the volume of their exports and the prices they were paid for the products they exported. Therefore, the preferential access granted by the European Communities to sugar from the ACP countries was vital to the economies of those countries and compensated, albeit to a limited extent, for the unfair terms of trade to which their underdeveloped economies were made subject.

5.41 Cuba, therefore, submitted that the starting point for consideration of this dispute should be the preambular provision of the Agreement on Agriculture, which states that "... in implementing their commitments on market access, developed country Members would take fully into account the particular needs and conditions of developing country Members by providing for a greater improvement of opportunities and terms of access for agricultural products of particular interest to these Members ...". Furthermore, Cuba submitted that the aim of these provisions on preferences was to foster the development of the ACP States in order to reduce and gradually eliminate poverty in those countries and integrate them into the mainstream of global trade. These objectives were consistent with WTO aims and principles and with the development dimension concept established at the Doha Ministerial Conference, which was the basic guideline for the current negotiations.

5.42 Fiji 296 noted that it had a substantial interest in this dispute, being a major producer and exporter of sugar to the European Communities under the Sugar Protocol. It explained that Fiji’s raw sugar exports to the European Communities constituted 40-50 per cent of its annual agriculture GDP or 12-15 per cent of its national GDP. Sugar earned between $250 to $300 million annually in foreign

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295 Third party oral statement by Côte d'Ivoire.
296 See also ACP statement in paras. 5.1-5.12 above.
exchange for the country. The ACP/EC Sugar Protocol and the more recent Special Preferential Sugar Agreement (SPS) for the importation of cane sugar, were an integral part of, and were fully incorporated within, the current EC sugar regime. The total quantity imported by the European Communities was 1,294,700 metric tons white sugar equivalent. Fiji's share of this agreed quantity was 165,348.3 metric tons white sugar equivalent. Some 60 per cent of Fiji's sugar exports were sold under the Sugar Protocol and the SPS Agreement. In the five preceding years, 1998-2002, sugar consistently accounted for between 83 per cent and 87 per cent of EC imports from Fiji.

5.43 Fiji claimed that special arrangements like the Sugar Protocol were specifically permitted under Article XXXVI (4) of the GATT. Referring to the text of that Article, Fiji was of the view that the market access and the guaranteed remunerative prices received for its sugar exports to the European Communities were indeed measures designed to assist ACP states, given the fact that they were dependent on one or two primary products, to earn foreign exchange that was critical to their social and economic development. These special arrangements were specifically permitted under the above provision of GATT 1994 and should be taken into consideration by the Panel in its determination of this dispute.

5.44 Referring to the Agreement on Agriculture, Fiji recalled that Article 15(1) specifically recognized that differential and more favourable treatment for developing country Members was an integral part of that Agreement. Furthermore, Fiji also asked the Panel to consider the implications on non-trade concerns (NTCs), in the terms of Article 20 (c) of the Agreement on Agriculture, that may result from the decisions the Panel take in this dispute. Fiji submitted that its longstanding trade preferences with the European Communities as regards its sugar exports under the ACP/EC Sugar Protocol were precisely the kind of trade preferences that should be protected under the multilateral trading rules of the WTO.

5.45 Fiji stressed that the various elements of the EC sugar regime (the "C" sugar, the intervention price, the 1.6 million tons of sugar allowed for exportation by the European Communities under the Uruguay Round, etc) were interlinked. If one aspect were to be undermined, the implications would spread to other elements. Once this happened, the coherency and the orderly management of the sugar regime would be lost and the very foundation and the fundamentals of the Sugar Protocol, under which Fiji sold its sugar to the European Communities, would be lost along with it.

5.46 Guyana emphasized that the various components of the EC sugar regime depended upon each other in so systemic a manner that the utmost care should be taken in attempting to rearrange its mechanism. To dismantle any particular aspect of the regime might tend to weaken and damage the very fabric of the preferential agreement: its quota system, its price structure, and its system of compensation. The possible impact of each proposed change should therefore be taken into account in assessing its overall implications in the world's trading system.

5.47 Guyana explained that its economy relied heavily on international trade. Imports exceeded the value of GDP, and the level of exports was not significantly lower. Of particular significance, however, was the fact that by far the greatest proportion of the country's exports was dependent upon preferential markets. Sugar and rice, both of which could not be sold competitively abroad without the existence of guaranteed markets and prices, dominated the traditional agriculture sector, accounting for nearly three-quarters of agricultural production, and almost one half of the total economy. Guyana's exports to the European Communities comprised over 90 per cent of the country's sales outside of the Caribbean, and fundamentally underpinned the nation's sugar industry and the entire economy of the nation. Twenty per cent of Guyana's GDP, and over 50 per cent of its

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297 Third party written submission and oral statement by Fiji.
298 See also ACP statement in paras. 5.1-5.12 above.
agricultural product, came from sugar. One out of every five persons in the entire population of Guyana was dependent upon sugar.

5.48 Guyana submitted that in the event of a successful challenge, the European Communities might be obliged to reform its sugar regime. This could result in a substantial reduction in the intervention price paid for preferential imports of raw sugar. For several reasons Guyana, like most ACP countries, would find it well-nigh impossible to enhance its productivity, in order to enable it to sell competitively in European markets. The removal or containment of sugar preferences in Guyana would have a most disastrous influence not only on the rural economies, but on the national economy as a whole. The collapse of preferences would lead to social and economic disintegration.299

5.49 India considered that this dispute was of great systemic importance not merely in terms of clarifying the rights and obligations of parties under the WTO Agreement on Agriculture but also in terms of its impact on the Doha Round. India noted that the Complainants had stated expressly that they had not raised any issues concerning the preferential access accorded by the European Communities to sugar of ACP and Indian origin. It recalled the statement in the preamble of the Agreement on Agriculture that "...[I]n implementing their commitments on market access, developed country Members would take fully into account the particular needs and conditions of developing country Members by providing for a greater improvement of opportunities and terms of access for agricultural products of particular interest to these Members, including the fullest liberalization of trade in tropical agricultural products as agreed at the Mid-Term Review...". The preferential access granted by the European Communities to the sugar of ACP and Indian origin had resulted in significant economic benefits especially to the ACP countries. India hoped, accordingly, that the preferential access to the EC market for sugar of ACP and Indian origin would not be undermined as a result of this dispute. At the same time, India appreciated the importance to the Complainants of ensuring genuine and speedy liberalization of agricultural export markets. India noted that rulings of the Appellate Body and of dispute settlement panels in Canada – Dairy had clarified that the term "payments" under Article 9.1(c) of the Agreement on Agriculture included both payments-in-kind to an exporter in the form of inputs that were sold at reduced prices;300 and where there was a single line of production, the financing of below cost-of-production exports through "highly remunerative prices" in the domestic market that fully covered total fixed costs.301

5.50 Whether a particular payment was financed by governmental action, India continued, must be assessed in terms of "governmental" action and involvement as a whole that permitted a transfer of resources to an exporting producer.302 India considered that the critical issue was whether "...governmental action was instrumental in providing a significant percentage of producers with the resources that enabled them to sell at below the costs of production".303 Further, export contingency existed because "[o]nly by contracting for export and effectively exporting [the agricultural product in question] can producers and processors engage in transactions outside he regulatory framework...applicable to domestic market...transactions...". In such a case, the payment is made 'on the export of an agricultural product”. It was not correct that the above principles would lead to confusing the distinction between domestic support and export subsidies. In India's view, where there was a single line of production and the quantities produced were to be sold in two separate markets, domestic support would result also in an export subsidy if two conditions were satisfied: (i) the regulatory framework ensured, for example, through domestic price support mechanisms and import barriers, that the revenue from domestic sales alone was large enough that the entire fixed costs of

299 Third party written submission and oral statement by Guyana.
production were covered; and (ii) there were quotas that limited the maximum amount that the producer could sell on the domestic markets and excess production must be exported.

5.51 If these conditions were satisfied, a rational farmer or processor of an agricultural product would certainly produce larger quantities of the product than could be sold on the domestic market provided that he had an outlet valve for the excess quantities in terms of exports particularly at prices that exceeded his marginal cost of production. Only by exporting the excess quantities could the farmer or the processor capture the entire benefit of this type of subsidy. In the context of this type of regulatory framework, therefore, Members in effect were extending export subsidies that were camouflaged as domestic support.

5.52 Further, India continued, once an Article 9.1(c) export subsidy was found to exist, it was almost inevitable that the foreign buyer of subsidized agricultural products could also be characterized as receiving a benefit passed on by the exporting producer. This did not mean, however, that the exporting producer had not received an Article 9.1(c) export subsidy.

5.53 With respect to the applicability of the SCM Agreement to subsidies for export of agricultural products, India stated that Article 13(c)(ii) of the Agreement on Agriculture acknowledged that an export subsidy that was not consistent with obligations assumed under the Agreement was actionable under Articles 3, 5 and 6 of the SCM Agreement. India also considered that, under Article 21.1 of the Agreement on Agriculture, the provisions of the SCM Agreement applied to an agricultural export subsidy that was not consistent with the provisions of the Agreement on Agriculture.

5.54 Referring to the principle of good faith, India recalled the Appellate Body ruling in EC – Computer Equipment, in which a Member’s schedule ordinarily was treated as part of the Agreement and the Agreement together with Members’ schedules represented the negotiated balance of concessions. Members often agree to become party to an agreement or to ratify it on the assumption that their schedules have been accepted by their trading partners in good faith. Therefore, India held that panels and the Appellate Body should hesitate to find that a conflict existed between a schedule and the substantive provisions of a covered agreement.

5.55 India believed that a clear distinction needed to be made under the Agreement on Agriculture between the following situations: one, where a Member made certain budgetary outlay and quantity commitments in respect of a product in its Schedule but failed to include certain export subsidies; and two, where a Member expressly specified in its Schedule, whether by way of a footnote or otherwise, that it was limiting its reduction commitments in respect of certain export subsidies. With respect to the first situation, by reading Articles 3.3 and 8 of the Agreement on Agriculture, India was of the view that if a Member made budgetary outlay and quantity commitments but failed to include in its schedule a particular type of subsidised export, it was prohibited from continuing to maintain such export subsidies to the extent that these exceeded either the budgetary outlay or quantity commitments contained in its Schedule. A plea by a Member that it had made a "scheduling error" based on an incorrect interpretation of Article 9.1(c) of the Agreement on Agriculture amounted to nothing more than confessing to a mistake of law. A mistake of law in turn could never be an excuse for failure to comply with a substantive treaty obligation. Further, the principle of good faith in public international law could not apply to excuse a Member who confessed to a mistake of law. Article 3.10 of the DSU could also have no application in this situation because it only required that a party should engage in dispute settlement under the DSU in good faith, not that a party's obligations under a 'covered agreement', as defined in Article 1.1 of the DSU, must be construed in accordance with its own mistaken interpretation of a particular provision of a covered agreement.

304 Ibid., para. 6 of India’s third party submission.
5.56 A plea of "scheduling error" attributable to a mistaken interpretation of the provisions of the Agreement on Agriculture must be distinguished, however, from the second situation referred to at the beginning of the previous paragraph. India submitted that a provision in a Member's Schedule, whether by way of a footnote or otherwise, that limited its export subsidy reduction commitments was consistent with the provisions of the Agreement on Agriculture. Based on its analysis of the provisions of the Agreement on Agriculture relevant to export subsidies, i.e. Articles 3, 8 and 9 of the Agreement on Agriculture, India noted inter-alia that in view of Article 8 a Member was under an obligation not to provide export subsidies except in conformity with the Agreement on Agriculture and in accordance with the commitments specified in its Schedule. It further noted that there was no definition in the Agreement on Agriculture of the term "reduction commitments" or any provision that specified the extent and scope of reduction commitments in respect of export subsidies that must be made by a Member for purposes of either Article 3.3 or Article 9.1. India argued that although sub-paragraph 2(b)(iv) of Article 9 provided for a reduction in a Member's export subsidies, this was only in the context of exceeding the budgetary outlay or quantity commitment levels specified in a Member's Schedule for the second through fifth years of the implementation period. It had no application where the Member's Schedule limited its export subsidy reduction commitments and did not undertake budgetary outlay or quantity commitments. Finally, India was of the view that the only understanding among Members on the extent of the reduction commitments was the "Modalities document", which in India's opinion, was not a covered agreement. Therefore, it could not be enforced through the DSU.

5.57 From this analysis, India inferred that Articles 3.3, 8 and 9.1 would not come into play where a Member had not made budgetary outlay and quantity reduction commitments in its Schedule or had expressly limited its export subsidy reduction commitments. India argued that where a Member had made budgetary outlay and quantity commitments in its Schedule in respect of export subsidies for a particular product, Articles 3.3 and 8 certainly required the Member to abide by these commitments.

5.58 Jamaica noted that sugar remained its most important agricultural export, contributing nearly 40 per cent of income earned from all agricultural exports. It continued to be Jamaica's most integrated agro-industry involving not only the cultivation of sugar cane, but also the manufacture of sugar, rum and molasses. Over 40 per cent of land in permanent agricultural cultivation was in sugar cane. It was estimated that nearly 200,000 persons or 8 per cent of the Jamaican population of 2.5 million benefited directly and indirectly from the industry.

5.59 The income earned from the export of sugar, primarily to the European Communities, was approximately US$78 million in the 2002/2003 season. The income earned was an important factor in Jamaica's interest in this dispute. The pricing mechanism which was the basis of this income was a primary element of the Sugar Protocol. A disruption of the pricing mechanism would have an adverse impact on the preferential arrangements covered by the Sugar Protocol and could lead to the demise of the industry causing high unemployment in rural areas, increasing the level of rural to urban migration and thus leading to serious social and economic dislocation.

5.60 With respect to the legal arguments and Jamaica's systemic interest, Jamaica noted that the Complainants and various third parties had argued that the burden of proof rested with the European Communities to prove that the amounts of sugar exported in excess of its reduction commitments had not been subsidised as required by Article 10.3 of the Agreement on Agriculture. But an analysis of WTO jurisprudence would show, Jamaica submitted, that this was only one aspect of the issue of burden of proof. The Complainants had the initial burden of proof to demonstrate that the European Communities' exports of sugar benefited from export subsidies in contravention of the European

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306 Third party written submission and oral statement by India.
307 See also ACP statement in paras. 5.1-5.12 above.
Communities' obligations under the WTO Agreement on Agriculture. According to Jamaica, WTO case-law required that the party who had the burden of proof must establish a prima facie case as discussed in the Appellate Body report on US – Shirts and Blouses and had been cited in practically all subsequent disputes when a burden of proof issue arose.

5.61 Referring to the panel report on India – Autos where it was established that if the party carrying the burden of proof did not manage to establish a prima facie case, the panel had no basis for a specific ruling on the issue at hand, Jamaica submitted that if the European Communities successfully rebutted the Complainants' arguments or simply provided submissions which balanced out those made by them, the Panel should rule in favour of the European Communities in line with the WTO jurisprudence.

5.62 With respect to the footnote in the EC Schedule, Jamaica was of the view that it was an integral part of the European Communities' commitments on sugar. Jamaica considered that the interpretation of the schedule did not form part of the Panel's terms of reference, but should the Panel consider this issue, a proper interpretation of the footnote in accordance with the general rules of interpretation of the Vienna Convention would allow the European Communities to export 1.6 million tons, with the benefit of export refunds, corresponding to its imports of ACP/Indian sugar.

5.63 Kenya noted that it was part of a large block of developing countries under the auspices of ACP countries whose partnership with the European Communities was geared towards a long-term objective of eradicating poverty and supporting development in the ACP countries. The ACP sugar exports to the European Communities created the requisite market access and formed part of the ACP/EC arrangement. Sugar is one of the few major commercial crops grown in Kenya. The average production area was estimated at 100,000 hectares, producing 4 million tons per year and employing over 200,000 small scale farmers. The sugar sector in Kenya was of vital importance as it contributed directly and indirectly to GDP in terms of employment, source of revenue to the government, foreign exchange earner, and poverty reduction and rural development.

5.64 The subsidy issue raised by the Complainants contested the very foundation on which the EC-ACP countries' arrangement was predicated and undermined the vision of eradicating poverty in developing countries such as Kenya. This arrangement had provided Kenya an assurance of stable prices and income to small scale farmers, not to mention investment in the sugar industry at a time when the flow of foreign direct investment have drastically diminished. Referring to Article 3.5 of the DSU, Kenya contended that the claim of the Complainants would have a detrimental effect on a large group of developing countries including Kenya as the Complainants had prima facie neglected the core principle therein.

5.65 Kenya noted that the European Communities and ACP waiver from the obligations of the European Communities under paragraph 1 of Article 1 of the General Agreement with respect to the preferential treatment for products originating in ACP states had been granted in good faith by all WTO members including the Complainants. The primary objective of this waiver was to safeguard the interests of ACP countries whose economies were heavily dependent on export of a few primary commodities. This, Kenya believed should be taken into account by the Panel. This waiver was fully consistent with the 1979 Decision on differential and more favourable treatment, reciprocity and fuller participation of developing countries in the multilateral trading system.

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310 Third party oral statement by Jamaica.
311 See also ACP statement in paras. 5.1-5.12 above.
5.66 Kenya recalled that agriculture formed the backbone of most of the ACP third party countries participating in this dispute. It also stressed the economic importance of the sugar industry in Kenya, and indeed in the ACP countries as it formed the cornerstone of the poverty reduction strategy of most of these countries.\textsuperscript{312}

5.67 Madagascar\textsuperscript{313} recalled the history of sugar cane production in Madagascar which started in 1917 at the instigation of the French colonial power. Already at that time, the production was export-oriented and the five production units developed then were the same ones today. These sugar industries were playing an essential role in the struggle against poverty in the country, constituting a the driving-force for the socio-economic development of the five regions in which these industries were situated.

5.68 Madagascar explained that the benefits from cane sugar growing was not limited to sugar production. Of the 2 million tonnes of cane produced annually, 900,000 tonnes were processed by the sugar industry; the rest went to the distillery industry or for other usages. Moreover, the sugar industry was a non-negligible employer with 3.82 per cent of the active population and 5.65 per cent of agriculture employment. The sugar industry assured also such services as health, education, roads and electricity since the State often did not have the appropriate budgetary means.

5.69 Recent inventories, Madagascar continued, had shown that the country had enormous potential in exploitable land for sugar cane production. Even though Madagascar suffered periodically from tropical hurricanes, its climate was favourable to sugar cane production, a fact recognized by foreign investors. Thus, sugar cane production assured not only a multifunctional role in the economy of Madagascar, but also a vital one. Therefore, Madagascar concluded, as a least developed country and producer and exporter of sugar, it was very concerned that a Panel decision would confirm the Complainants allegations. Access to the EC market, at guaranteed prices, was the key to sustained development of the sugar industry and its "satellites".\textsuperscript{314}

5.70 Malawi\textsuperscript{315} noted that it was a least developed, landlocked country whose economy was heavily dependent on commodities such as sugar. It submitted that the sugar industry played a very vital developmental role by providing employment and other social services such as health, education, housing, and infrastructure. Furthermore, the sugar industry had led to the socio-economic transformation of the rural areas where the sugar industry was located, resulting in the growth of small townships actively engaged in trading and other related activities. Small scale businesses had developed which provided services to the industry and its employees.

5.71 The economic importance of the sugar industry in Malawi's socio-economic development and its positive impact in the fight against poverty was demonstrated by the fact that it employed directly more than 15,000 people in the field and factory operations. Directly and indirectly the sugar industry was responsible for the livelihood of over 95,000 people. Since the introduction of the preferential treatment under the Sugar Protocol to which Malawi became a beneficiary, sugar had replaced tea to rank second only to tobacco as a major foreign exchange earner. The ACP/EC sugar regime provided the necessary price stability and predictability for attracting investment. The industry was now floated on the local bourse, affording Malawians an opportunity to own shares.

5.72 The foreign exchange revenue from sugar exports had contributed significantly to the government budget by broadening both the corporate and income tax base. Needless to say the industry had become an important contributor to Malawi's GDP.

\textsuperscript{312}Third party oral statement by Kenya.
\textsuperscript{313}See also ACP statement in paras. 5.1-5.12 above.
\textsuperscript{314}Third party oral statement of Madagascar.
\textsuperscript{315}See also ACP statement in paras. 5.1-5.12 above.
5.73 Malawi noted that it had for a long time depended on tobacco as the predominant foreign exchange earner and for its development. However, tobacco was experiencing a great deal of problems as a result of the global anti-smoking lobby. Malawi therefore needed to diversify its economy and sugar provided the most viable alternative. All these were huge challenges for a small landlocked, commodity dependent LDC. For Malawi to be economically viable and for it to graduate to the next level of development, it had to continue making huge sacrifices. The outcome of this challenge could therefore very well determine how Malawi would confront and succeed in its development efforts amidst these daunting challenges. Only a positive outcome would guarantee Malawi’s competitiveness in its trade and trade related activities.\textsuperscript{316}

5.74 Mauritius\textsuperscript{317} explained that the sugar industry had a multifunctional role in Mauritius, having both an economic impact as well as a socio-economic, energy and environmental impact. Mauritius noted that 50 per cent of the land area in the country was devoted to agriculture, 90 per cent of which was used for sugar cane production. Also, 90 per cent of agricultural export proceeds came from sugar exports with gross sugar export earnings amounting to some US$330 million or some 20 per cent of all merchandise exports. The net sugar export earnings covered 75 per cent of the food import bill in a country that had to import nearly all of its food requirements; this food procurement capacity, Mauritius submitted, was vital for its food security.

5.75 Furthermore, some 200,000 persons were directly or indirectly dependent on the sugar sector for their livelihood, out of a population of 1.2 million, and sugar proceeds were used to provide key services such as research and insurance to the industry. Electricity generated by sugar factories or power plants using bagasse, Mauritius continued, an environment friendly renewable source of energy, represented 25 per cent of the national production. The use of bagasse in an island devoid of fossil fuels was a key element of the energy strategy. With respect to the environmental impact of the sugar industry, Mauritius observed that the cane plant was by far the most important carbon sequestrator of all cultivated plants. The high yield per hectare of cane helped to mitigate the enhanced greenhouse effect.

5.76 Mauritius had remained largely a single-commodity exporter, not out of choice but as the result of the inherent constraints the country faced as a small island state located in a cyclonic belt. In view of the overall importance of the sugar industry, any disruption of the EC sugar regime would result in a significant fall in Mauritius export earnings and would severely damage the island’s fragile economy, social fabric and environment.

5.77 Mauritius submitted that the sugar exports of Mauritius or other ACP sugar-supplying states to the European Communities did not affect the balance of interests established between the various stakeholders under the EC sugar regime. Though the ACP exports to the European Communities have since 1975 increased from 1.3 million tonnes to 1.6 million tonnes, they could not be deemed to create any market distortion. The ACP/EC sugar trade agreement was an important pillar of the EC sugar regime and any ruling in favour of the Complainants could only jeopardise the survival of the economy of Mauritius and of other ACP States.\textsuperscript{318}

5.78 New Zealand referred to the Appellate Body report in Canada – Dairy and argued that in the context of Article 9.1 (c), "payment" included revenue foregone.\textsuperscript{319} To determine whether a payment had been made "requires a comparison between the price actually charged by the provider of the goods or services… and some objective standard or benchmark which reflects the proper value of the

\textsuperscript{316} Third party oral statement by Malawi.

\textsuperscript{317} See also ACP statement in paras. 5.1-5.12 above.

\textsuperscript{318} Third party oral statement by Mauritius.

\textsuperscript{319} Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US), para. 73.
goods or services to their provider...". The "objective standard or benchmark" identified by the Appellate Body in *Canada – Dairy* was the average total cost of production. Accordingly, where a producer sold a product at less than it cost to produce it, there was a "payment" within the meaning of Article 9.1(c). New Zealand held that the Complainants had provided factual evidence demonstrating that the producers of C sugar were charging a price for their exports that was below the average total cost of production of C sugar and that the European Communities had produced no evidence to the contrary. Nor had it sought to provide an alternative benchmark to that of the average total cost of production, as applied in *Canada – Dairy*. There was, therefore, a "payment" in the context of Article 9.1(c). The attempt by the European Communities to suggest that this conclusion should turn on whether or not there was an intermediary involved in the export of sugar had no basis in logic, and no foundation in law.

5.79 New Zealand stressed that, unlike what was argued by the European Communities, there was no need to demonstrate the existence of a "benefit" within the meaning of Article 1.1(b) of the *SCM Agreement* in order to satisfy the requirements of Article 9.1(c) of the *Agreement on Agriculture* since the terms of Article 9.1(c) established a "stand alone" definition of an export subsidy that could be given effect on its own terms, as it had in the *Canada – Dairy* dispute. In any case, even if such a "benefit" needed to be demonstrated, one clearly exists. Producers can export "C" sugar without making a loss (indeed in doing so they make a profit) because they need only cover their marginal costs, and thus receive a benefit.

5.80 New Zealand concurred with the Complainants that the payments on C sugar were dependent or conditional upon the C sugar being exported. If the C sugar was not exported, no payments were made (there was no revenue foregone). C sugar could only be exported – it could not be sold on the domestic market. C sugar was also not eligible for Article 9.1(a) export subsidies. Nor could C sugar viably be exported in the absence of the payment. When the option was exercised of carrying over the C sugar to the next marketing year where it could be reallocated as 'A' sugar and either sold at the high domestic price or exported with the benefit of Article 9.1(a) export subsidies, no payment in the context of Article 9.1(c) would be made.

5.81 New Zealand questioned the European Communities' argument that the requirement of export contingency applied to the measures that financed the payments, rather than to the payments themselves. In the opinion of New Zealand, Article 9.1(c) requires that it is the "payments" that must be "on the export" and not the governmental action which finances them. Moreover, New Zealand argued, there was no requirement to show that the operation of the European Communities' domestic price support mechanisms were contingent upon the export of C sugar. What was required and which New Zealand believed had been demonstrated by the Complainants, was that the payments to C sugar were contingent upon C sugar being exported.

5.82 Finally, New Zealand asserted that if the European Communities were to "remove the condition" that required C sugar to be exported, then the Article 9.1(c) export subsidy would indeed no longer be in place. There would be nothing in such an action requiring the European Communities to cease supporting its domestic production. Therefore, New Zealand rejected the European Communities' claim that the Complainant's interpretation of Article 9.1(c) would blur the distinction between the disciplines on domestic support and export subsidies.

5.83 With respect to "financed by virtue of governmental action", New Zealand referred to the reasoning developed by the Appellate Body in the *Canada – Dairy* dispute, in which it was required to establish the existence of a demonstrable link between the governmental action at issue and how

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320 Ibid., para. 74.
321 European Communities' first written submission, para. 42.
322 European Communities' first written submission, para. 64.
payments were financed. New Zealand argued that, as was the case in Canada – Dairy, producers could cover their fixed production costs through sales of 'A' and 'B' quota sugar and needed to cover only the marginal costs of C sugar production on sales in the export market. In this way the domestic sales of 'A' and 'B' sugar cross-subsidised exports of C sugar that would otherwise not occur or be made at a loss. New Zealand believed, as demonstrated by the Complainants, that governmental action created both the means and the incentive for this cross-subsidisation to occur and exports of C sugar to be made. Governmental action was inherent throughout the tight regulatory controls that the European Communities exercised over every aspect of sugar production in the European Communities. Those controls set guaranteed prices for 'A' and 'B' sugar production for the domestic market. The high domestic prices offset some of the cost of C sugar production, which was further encouraged by other aspects of the regime. Thus, for New Zealand, there was clearly a "demonstrable link" between the relevant "governmental action" and the means by which "payments" were financed.

5.84 In the alternative, New Zealand submitted, the European Communities' sugar regime provided export subsidies not listed in Article 9 resulting in circumvention of the European Communities' export subsidy commitments contrary to Article 10.1 of the Agreement on Agriculture. New Zealand considered that the Complainants had demonstrated that the EC sugar regime provided an export subsidy as described in paragraph (d) of Annex I to the SCM Agreement. As the Appellate Body had confirmed, the Illustrative List in Annex 1 to the SCM Agreement provides a list of practices considered to be "export subsidies" under the SCM Agreement and thus, if a measure was described in the Illustrative List it may be characterised as an "export subsidy" within the meaning of Article 10.1.

5.85 As regards the applicability of the SCM Agreement, in New Zealand's view the words "Except as provided in the Agreement on Agriculture" had the effect of applying the prohibitions on the subsidies set out in Article 3 of the SCM Agreement except where such subsidies were expressly permitted by the Agreement on Agriculture. This approach reflected the fact that the Agreement on Agriculture provided a limited and clearly delineated authorisation to Members to provide subsidies in respect of agricultural products that would otherwise not be permitted.

5.86 Referring to the European Communities' argument with respect to impairment or nullification, New Zealand held that the issue in this dispute was whether the benefit accruing to Members under Articles 3.3, 8 and 10.1 of the Agreement on Agriculture, was adversely impacted by the European Communities' breach. As recognized by the European Communities, Articles 3.3, 8 and 10.1 protect an expectation as to the competitive relationship that would exist between the exports of one Member and those of another. Accordingly, there was no reason, in New Zealand's view, to reach a different conclusion from that reached in US – Superfund that "a change in that competitive relationship contrary to [the provisions of the Agreement on Agriculture] must consequently be regarded ipso jacto as a nullification or impairment of benefits accruing [under the Agreement on Agriculture]." Furthermore, New Zealand did not believe there was any requirement to show "injury", which had a specific meaning in the context of WTO law.

5.87 As concerns exports of ACP/India equivalent sugar and reduction commitments, New Zealand sustained that there was no option in the Agreement on Agriculture whereby Members could cap the volume of an Article 9 export subsidy. Thus, subsidies on the export of 1.6 million tonnes of ACP/India equivalent sugar could only be provided subject to reduction commitments.

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324 European Communities' first written submission, para. 145.
325 Ibid., para. 148.
327 Third party written submission and oral statement by New Zealand.
5.88 **Paraguay** considered that the assistance granted by the European Communities to its Member States was at odds with the multilateral provisions of the *SCM Agreement* and the *Agreement on Agriculture* as well as with the rules of the GATT 1994. For the purposes of this dispute, given that not only was this assistance distorting international trade, but the distortion was, in the opinion of Paraguay, particularly damaging to the developing countries, Paraguay submitted that there was a violation of rules and principles as well as adverse effects on trade which were seriously injuring the economy and development, in this case of Paraguay.

5.89 As regards inconsistency with the *Agreement on Agriculture*, Paraguay noted the effects on the export and competitiveness of the product at issue in the international market, which were, in Paraguay's opinion, inconsistent with Articles 3.3 and 8 of the Agreement. Paraguay deemed it important to consider Article 8 of the *Agreement on Agriculture* with respect to domestic policies that jeopardize export competition. That article clearly lays down the obligation for each Member to refrain from providing export subsidies otherwise than in conformity with the Agreement and with commitments as specified in that Member's Schedule.

5.90 Paraguay held that the commitments not to provide export subsidies in accordance with the conditions set forth in Article 8 of the *Agreement on Agriculture* assumed that there would be individual cases in which countries were free to apply domestic support mechanisms (in this case a subsidy). Such freedom was contingent upon policies to encourage agricultural and rural development in the developing countries as part of agricultural programmes for low-income or resource-poor producers. In such cases, developing countries were entitled under the WTO not to reduce their domestic support (Article 6 of the *Agreement on Agriculture*). In the case at issue, the subject of the dispute clearly did not reflect the situation described above. This was why, as stated by the Complaining parties, the European Communities appeared to be violating Articles 3.3 and 8 of the *Agreement on Agriculture*. Indeed, in the circumstances described, the granting of the export subsidy applied to a quantity of sugar that exceeded the level of its support reduction obligations.

5.91 Paraguay explained that it was a country faced with an urgent need to increase the volume of its exports, in particular its agricultural exports. The Sugar protocol imposed obstacles or difficulties in exercising what Paraguay considered as its genuine right of access to larger markets. In this sense, Paraguay was of the view that the European Communities must comply with the provisions of the *Agreement on Agriculture*, bearing in mind that the export subsidies granted to the European countries in question were inconsistent with Articles 3.3 and 9.1 of that Agreement.328

5.92 **St Kitts and Nevis**329 explained that sugar and molasses accounted for as much as 92.3 per cent of the islands total agricultural exports as well as for 58.2 per cent of the total number employed in agriculture, which was indicative of the country's high dependence on sugar. St. Kitts and Nevis was classified as a Small Island Developing State and was the smallest independent State in the Americas, and also the smallest member both in terms of size, population and volume of trade, of the WTO.

5.93 St. Kitts and Nevis was also a traditional sugar exporter with no realistic opportunity for diversification of the agricultural sector which was defined in terms of a single agricultural export – sugar – to a single export market – the European Communities. St. Kitts and Nevis exported some 15,000 tonnes per year to the European Communities. Sugar exports to the European Communities represented a vital source of foreign exchange, a major source of rural employment and income, and given the multi-functionality of sugar, it was of great social, economic and environmental importance to St. Kitts and Nevis. The country was also a net food importing country and agricultural production on sugar estates helped alleviate this situation.

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328 Third party written submission and oral statement by Paraguay.
329 See also ACP statement in paras. 5.1-5.12 above.
5.94 St. Kitts and Nevis submitted that the ACP third party submission and statement had demonstrated the unique arrangements which comprised the EC sugar regime. This regime was based on a system of guarantees which were dependent upon each other in so systemic a manner that any rearrangement or dismantling of any aspect of that regime would likely lead to a collapse of the entire system. The EC Sugar Protocol, from which the preferential arrangements derived, had become enshrined in international treaty obligations and had been sanctioned by WTO rules and laws and, indeed, St. Kitts and Nevis noted, the Complainants were among the GATT Members which reviewed the Sugar Protocol and agreed to grant it a waiver from Article I of the GATT. The Complainants therefore knew or ought to have known that one of the objectives of the Sugar Protocol was the reduction and eventual eradication of poverty, consistent with sustainable development and the gradual integration of the ACP countries into the world economy. St. Kitts and Nevis therefore found it troubling that at this late stage, the Complainants were trying to claw back benefits that had been conceded to the ACP.330

5.95 Swaziland331 noted that it was a small and vulnerable landlocked developing country heavily dependent on the production and export of sugar, relying on the predictable and stable earnings from sugar exports to the European Communities under the ACP/EC trading arrangements on sugar for addressing specific economic and social difficulties and for sustainable economic development in general. Sugar was the most important pillar of the Swazi economy. With the recent expansion into smallholder agricultural schemes, it had brought significant relief to the government's policy objective of poverty reduction and played a key role in supporting key sectors of the economy such as transport, finance, water and electricity.

5.96 In a normal year, sugar cane production contributed 61 per cent to agricultural output which in turn was 11 per cent of GDP. Sugar's contribution to agriculture rose to 75 per cent during periods of drought. For Swaziland, sugar was and would remain the predominant agricultural activity. But, due to geography and climate, Swaziland could not become a world class multi-commodity exporter even in the foreseeable future. Sugar exports provided much-needed foreign exchange earnings for the Swazi economy. In 2002, export earnings derived from sugar sales accounted for 7 per cent of the country's total export earnings and 36 per cent of total agricultural export receipts. These export earnings were used inter-alia to finance development programmes, rationalisation and modernisation programmes in the sugar industry as well as diversification in other sectors. Sugar exports to the European Communities represented more than one-third of the country's sugar production and a much higher proportion of the sugar revenue, divided between millers and growers in accordance with an agreed formula.

5.97 Furthermore, Swaziland explained, the sugar industry was a major employer, accounting for more than 9 per cent of the working population. It was estimated that the sugar industry provided support to about 85,000 people (9 per cent of the total population of just over 1 million). It accounted for 92 per cent of total agricultural employment. A positive externality that had resulted from the growth of the sugar industry was its contribution toward the achievement of the Government's objectives of poverty reduction through the provision of social services to the population. The Swazi sugar industry had invested substantially in housing, education (kindergarten, primary and secondary), health care services, recreational facilities and clean water. These benefits had been extended beyond the sugar industry's precincts to the surrounding rural communities. In addition, the sugar growing areas had attracted other support businesses such as finance, transport and retail trade.

5.98 Although sugar exports from Swaziland and other ACP countries comprised an insignificant amount of global sugar trade and did not affect the market shares of large sugar exporters like the Complainants in this dispute, they played considerable roles in their respective economies. Due to the

330 Third party oral statement by St Kitts and Nevis.
331 See also ACP statement in paras. 5.1-5.12 above.
fragile and vulnerable nature of its economy, Swaziland would not be in a position to absorb precipitous changes without serious disruptions in its socio-economic stability. As a narrowly based economy, which was difficult to diversify, Swaziland could not absorb changes in the same time scale as more developed and broadly based economies.

5.99 Swaziland considered that a ruling in favour of the Complainants would be devastating for its fragile economy. It would result in a drastic reduction in the level of economic activity in a country where two-thirds of the population lived below the poverty line. Swaziland concluded that the consequences of the ruling in favour of the Complainants in this dispute would be much against the spirit of the ACP/EC Partnership Agreements and the objectives set out in the Preamble of the Marrakech Agreement, as well as the objectives of the GATT and WTO.\footnote{Third party oral statement by Swaziland.}

5.100 Tanzania\footnote{See also ACP statement in paras. 5.1-5.12 above.} was of the view the Sugar Protocol was anchored in a moral imperative to create a special opportunity that could support the development aspirations of ACP countries, among whom were some of the world’s weakest and most vulnerable nations. Unlike Australia, Brazil and Thailand, Tanzania remained one of the world’s poorest countries classified as LDCs. The economy was weak, dominated by agriculture which made up about 60 per cent of the GDP, 85 per cent of total export earnings and employed 90 per cent of the active labour force. Over 90 per cent of Tanzania’s agriculture relied on smallholder peasants. Topography and harsh climatic conditions limited crop production to less than 4 per cent of the total land area.

5.101 The Industry sector, which accounted for only 10 per cent of Tanzania’s GDP, was one of the smallest in Africa and the world. About 50 per cent of the manufacturing industry was agro-based, including sugar. Its contribution to exports was small, because of Tanzania’s low capacity to penetrate international markets and compete with big suppliers, including those of sugar. The modest quantities of sugar that Tanzania did export were actually thanks to the EC/ACP Sugar Protocol.

5.102 Under the EC sugar arrangements, Tanzania explained, it did not only benefit from the preferential export market and remunerative prices, but also derived greater investment and employment opportunities, which were crucial for the economic and social transformation of the country. Consequently, after a three-decade period of setbacks, sugar production was increasing, along with exports. Tanzania’s sugar production was expected to increase from 190,120 tonnes last year, to 245,000 tonnes this year. On the other hand, sugar exports to the EC markets increased from 22,150 tonnes in 2001/2002, to 22,700 tonnes in 2002/2003. The turnaround had also expanded employment opportunities to a large number of smallholders and professionals.\footnote{Third party oral statement by Tanzania.}

5.103 Trinidad and Tobago\footnote{See also ACP statement in paras. 5.1-5.12 above.} submitted that the European Communities’ sugar regime and the Sugar Protocol were symbiotically linked. An attack on any one area of this special arrangement would have a deleterious effect on the entire structure. Trinidad and Tobago was fully cognizant of the multifunctional role of agriculture particularly in rural communities. For Trinidad and Tobago, agriculture was more than a trade activity in which market access was actively pursued. Agriculture contributed to the very social and cultural fabric of our communities. The sugar industry promoted and supported other commercial activities, provided infrastructure, and recreational facilities and more importantly, by its very presence, limited rural exodus through the provision of meaningful employment. Further, in Trinidad and Tobago, sugar cane cultivation was practised primarily by small farmers. A loss of market share or preferential access would negatively affect and displace not only these cane farmers, but also employees, other stakeholders and residents in surrounding
communities where cane farming and production was prominent. It was the benefits derived from preferential access that permitted the continuation of the aforementioned activities.

5.104 In Trinidad and Tobago's view, the two primary benefits derived from the Sugar Protocol's preferential quota arrangements were the guaranteed access and the remunerative prices. The Sugar Protocol had in effect reduced the instability of export earnings and had been an important source of both price stability and sales security for sugar producers. Trinidad and Tobago's current quota under the Sugar Protocol was 45,404 tonnes of raw sugar while that under the Special Preferential System (SPS) it was 7,385 tonnes. For the period 1994–2002, Trinidad and Tobago's shipments of Protocol sugar averaged 38 per cent of the country's total sugar production and 84 per cent of its total sugar exports. In 2003, according to the provisional figures provided by Trinidad and Tobago's statistical authorities, the earnings of the sugar industry were assessed at TT $328 million (approximately US $52 million). For Trinidad and Tobago, this was a significant sum and it represented approximately 43 per cent of the total earnings of the agriculture sector.

5.105 Trinidad and Tobago had embarked on a path of restructuring and reorganization of its sugar industry, the intent being that there be less governmental intervention. As a result of the restructuring, the number of cane farmers and those involved in related activities had been substantially reduced with its social and economic consequences. Trinidad and Tobago noted that the preferential arrangements were one of the pillars on which the restructured industry had been built. Referring to the preamble of the Marrakech Agreement Establishing the World Trade Organization, Trinidad and Tobago was of the opinion that the present challenge to the ACP/EC preferential trading arrangement on sugar could result in the substantial reduction or complete elimination of Trinidad and Tobago's sugar industry, i.e. the very opposite of the objectives in the preamble would most likely be realised.  

5.106 The United States noted that it took no view as to whether, under the facts of this dispute, the measures at issue were consistent with the Agreement on Agriculture and/or the SCM Agreement. However, the question was whether the European Communities was providing export subsidies for C Sugar, a question that needed to be resolved by reference to the text of the Agreement on Agriculture and the SCM Agreement. If the answer was that the European Communities was providing export subsidies for C sugar, then the question would be whether the European Communities was exceeding its export subsidy commitments for sugar. And that was a question that needed to be resolved with reference to the Agreement on Agriculture and the EC's Schedule.  

5.107 In response to the European Communities' arguments that, first, it was known at the time it negotiated its Schedule that C sugar did not receive export subsidies and, therefore, it was known that the European Communities did not include C sugar in the base quantity for calculation of its reduction commitments; and second, that the modalities guidelines developed during the negotiations supported the European Communities' position that, if the Panel concluded that the European Communities was exceeding its commitments, the European Communities' commitment levels for sugar export subsidies should be recalculated, the United States was of the opinion that neither of these arguments could be used to contradict the text of the WTO Agreement.

5.108 The United States, referring to the European Communities' argument with respect to what was "known" at the time the European Communities negotiated its Schedule, considered that this was not the issue. Members' alleged "knowledge" did not govern the legal inquiry, but rather it was the Members' agreement, reflected in the text of the WTO Agreement, that governed. Similarly, the United States recalled that the modalities guidelines were not a covered agreement, indeed were not

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336 Third party oral statement of Trinidad and Tobago.
337 Third party written submission of the United States, para. 3.
an agreement at all, and did not provide "context" for interpreting the text of the WTO Agreement.\(^{338}\)

It stressed that the modalities document itself established that it was not a covered agreement.\(^{339}\)

5.109 In this respect, the United States recalled the Appellate Body report in EC – Bananas III, in which the Appellate Body made the observation that the modalities paper was not referred to in the Agreement on Agriculture.\(^{340}\) The United States also contended that Members had explicitly rejected the modalities guidelines as "context" for interpreting Member Schedules. The United States was further of the view that it was not necessary, in this case to have recourse to supplementary means of interpretation as set out in Article 32 of the Vienna Convention.

5.110 Accordingly, to determine whether the measures at issue constituted export subsidies for purposes of the Agreement on Agriculture, it was necessary to refer to the definition of export subsidy in that Agreement and related provisions. Similarly, it would be necessary to refer to the definition and related provisions in the SCM Agreement to determine if the measures were export subsidies for purposes of that Agreement. If the measures were export subsidies, the United States continued, and were in excess of the European Communities' export subsidy commitments, then the European Communities would need to bring its measures into compliance. Additionally, the measures would be subject to the SCM Agreement disciplines.

5.111 The United States was of the view that, contrary to what the European Communities was alleging, the FSC dispute showed that subsidies could be analyzed under both the SCM Agreement and the Agreement on Agriculture. Contrary to the European Communities' assertion, the United States noted that the Canada-Dairy dispute also did not stand for the proposition that a measure could not be analysed under both agreements. This was not to say, however, that the SCM Agreement applied to all agricultural support or subsidies. Rather, the question needed to be approached on a provision-by-provision, case-by-case basis. Such an interpretation was supported by the language of Article 3 of the SCM Agreement, which states that certain subsidies are prohibited "except as provided in the Agreement on Agriculture". If export subsidies did not fully conform to the commitments established under Part V of the Agreement on Agriculture, those subsidies were subject to the SCM Agreement disciplines.

5.112 With respect to export contingency, the United States recalled that in Canada – Dairy, the panel had found, in a statement not modified by the Appellate Body, that Canada's payments were made contingent on the export of the agricultural product at issue.\(^{341}\) This critical aspect of government intervention – export contingency – was found because Canada's governmental scheme mandated that products for which payments were received had to be exported. Thus, governmental intervention requiring export performance was a necessary part of any analysis of the obligations under Article 9.1(c) of the Agreement on Agriculture. In the opinion of the United States, this export contingency requirement applied to both the Agreement on Agriculture and the SCM Agreement.

5.113 With respect to the discussion of the role of international law, particularly concerning the concept of estoppel, the United States reiterated that Article 1.1, Appendix 1, and Article 3.2 of the DSU reflected a very conscious choice on the part of WTO Members to limit the use of international law in WTO dispute settlement proceedings to customary rules of interpretation. Members had not consented to provide for the application of the principle of estoppel in WTO dispute settlement. No provision of international law as such, the United States continued, was a "covered agreement" that

\(^{338}\) Third party written submission of the United States, para. 4.

\(^{339}\) Modalities for the Establishment of Specific Binding Commitments, MTN.GNG/MA/W/24 (20 December 1993) (Exhibit EC-3).


may be applied in WTO dispute settlement, nor was there any other basis for importing into the WTO other provisions or obligations of public international law.

5.114 The lack of any textual basis for importing the principle of estoppel, the United States continued, was further emphasized by the lack of consistent description of the concept when panels had had occasion to discuss estoppel in the past. In *EEC (Member States) – Bananas I*, for example, the panel stated that estoppel can only "result from the express, or in exceptional cases implied, consent of the complaining parties." In *EC – Asbestos and Guatemala – Cement*, by contrast, the panels stated that estoppel was relevant when a party "reasonably relies" on the assurances of another party, and then suffers negative consequences resulting from a change in the other party's position. These inconsistencies illustrated the dangers of seeking to identify purportedly agreed-upon legal concepts beyond the only source all Members had agreed to – the text of the *DSU* itself.

VI. INTERIM REVIEW

6.1 On 17 August 2004, pursuant to Article 15.2 of the *DSU*, Article 16 of the Panel's Working Procedures and the revised Timetable for Panel Proceedings, the parties provided their comments on the Interim Reports. None of the parties requested a meeting to review part(s) of the Interim Reports. On 24 August 2004, pursuant to the revised Timetable for Panel Proceedings, the parties submitted further written comments on the comments that had already been provided on the Interim Reports on 17 August 2004.

6.2 In light of the parties' interim comments, the Panel has reviewed its Findings. Pursuant to Article 15.3 of the *DSU*, this section of the Panel Reports contains the Panel's response to the main comments made by the parties in relation to the Interim Reports and forms part of the Findings of the Panel Reports.

A. EDITORIAL AND OTHER CHANGES

6.3 The parties have suggested a number of editorial changes to the Interim Reports and corrections of typographical errors; parties have also suggested different ways to present their arguments and have sometimes requested that references be added to specific arguments or specific exhibits or that factual statements made by the Panel be deleted. The Panel has largely accepted these suggestions and revised its findings accordingly.

B. TERMS OF REFERENCE

6.4 The European Communities considers that its objections concerning the scope of the terms of reference should be dealt with by the Panel separately with respect to each complaining party, taking into account exclusively what is stated by each complaining party in its own panel request and the arguments/claims made by each of them during the proceedings and the moment at which they were made for the first time by each of them.

6.5 The Panel agrees with the European Communities that each of the Complainants' panel requests must comply with the requirements of Article 6 of the *DSU*. Moreover, while the three disputes dealt with the same matter and were joined pursuant to Article 9 of the *DSU*, Article 9.2

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342 See Panel Report on *Argentina – Poultry Anti-Dumping Duties*, para. 7.38 (quoting *EEC (Member States) – Bananas I*).


344 Third party oral statement of the United States, para. 9.
makes clear that in such circumstances the Panel has to ensure "that the rights which the parties to the dispute would have enjoyed had separate panels examined the complaints are in no way impaired".

6.6 In the Panel's view, although the complaining parties drafted their panel requests using slightly different terms,345 each of the Complainants' panel requests has identified essentially the same measures - subsidies accorded under EC Council Regulation 1260/2001 under the so-called EC Sugar regime - and the same alleged violation - the European Communities exceeds its budgetary outlays and quantity commitments contrary to Articles 3 and 8 of the Agreement on Agriculture. For this reason, after noting the specific language of each panel request, and in light of the fact that the Complainants endorsed each other's factual and legal arguments, the Panel was able to examine the European Communities' allegations concerning the Panel's terms of reference and whether some of the Complainants' arguments could be validly invoked in the course of the present proceedings.

6.7 In particular, the European Communities has argued that each payment discussed by the Complainants constitutes a distinct claim and all these claims (alleged payments) have not been specifically identified in each of the Complainants' Panel requests - and for the European Communities this lacuna cannot be cured by the allegation during the panel process that all Complainants endorsed each other's arguments.

6.8 The Panel agrees with the European Communities that the Complainant's claims must be adequately specified in each of the Complainants' Panel requests. The legal basis of the Complainants' claims is Articles 3 and 8 of the Agreement on Agriculture. The Panel is of the view that a claim under Article 3 (and Article 8) of the Agreement on Agriculture requires allegations that, first, the European Communities has exported sugar above its commitment levels and, second, that such exports of sugar were subsidized. In the Panel's view, the Complainants have satisfied these requirements adequately. In their requests for establishment of a panel, the Complainants did not have to detail how and why such exports were being subsidized, only that the commitment levels were exceeded and that exports were subsidized. Moreover, the Complainants did indicate some aspects of the export subsidization of EC sugar in their panel requests in referring to Article 9.1(a) and 9.1(c) of the Agreement on Agriculture.

6.9 Therefore, the Panel considers that the Complainants' Panel requests complied with the requirements of Article 6.2 of the DSU in that they adequately identified the measures at issue and the violations claimed to have occurred, i.e. that the European Communities' exports of subsidized sugar exceeded the European Communities' commitment level contrary to Articles 3 and 8 of the Agreement on Agriculture. They further developed in their written or oral submissions argumentation as to how and why in their view, exports of C sugar are subsidized. In the Panel's view, the European Communities understood these claims from the beginning of the DSU process and articulated its defence accordingly.

C. THERE ARE NO "C SUGAR PRODUCERS" AND NO "C BEET GROWERS" AS SUCH

6.10 Australia suggests that the references to "C beet growers" and "C sugar producers" are inaccurate in that this terminology implies that there are enterprises engaged solely in the growing/farming of C beet and enterprises engaged solely in the production of C sugar. Australia emphasises that the "growers of C beet are also growers of A and B beet" that is, there is no independent production of C beet. Moreover, the producers of C sugar are the same companies that produce A and B sugar, that is, there is no independent production of C sugar.

6.11 The Panel is aware of the fact that strictly speaking there are no "C sugar producers" as such; there are no sugar producers that produce only C sugar. C sugar is produced by the producers of A

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345 See the full text of the panel requests in Annex D below.
and B sugar. Therefore "C sugar producers" are EC sugar producers who produce C sugar in addition to A and B sugar. The same is true for C beet. There are no beet farmers who grow only C beet. C beet is grown by farmers of A and B beet. Therefore "C beet growers" are the EC beet farmers who also grow C beet, in addition to A and B beet. The Panel has tried to make this clear in footnote 544 of its Panel Reports. In the present dispute, the Panel has had to assess whether the exports of sugar in amounts exceeding the European Communities' scheduled commitment levels are subsidized. The Panel understands that the exceeding sugar is composed of C sugar and ACP/India equivalent sugar. In its assessment of whether exports of C sugar are subsidized, the Panel examines the costs of growing C beet as well as the costs of processing and producing C sugar. In doing so the Panel refers to C beet growers and C sugar producers with a view to focussing on the exports of sugar that are above the European Communities' commitment levels.

D. A REFERENCE TO THE EUROPEAN COMMUNITIES’ COMMITMENTS FOR BUDGETARY OUTLAYS

6.12 Australia has requested that the Panel clarifies in its conclusions that Footnote 1 to Section II, Part IV of the European Communities' Schedule does not enlarge or otherwise modify the European Communities' specified quantity commitment of 1,273,500 tonnes per year, nor does it modify or enlarge the European Communities' specified budgetary outlays.

6.13 The Panel agrees with Australia and has clarified its findings and conclusions so that it is now clear that the European Communities' annual budgetary outlay and quantity commitment levels for exports of subsidized sugar are determined with reference to the entries specified in Section II, Part IV of its Schedule and that the content of Footnote 1, in relation to these entries, is of no legal effect and does not enlarge or otherwise modify the European Communities' specified commitment levels.

E. PANEL’S EXERCISE OF JUDICIAL ECONOMY OVER THE SCM CLAIMS

6.14 Australia requested the Panel to reconsider its decision to exercise judicial economy in regard to findings under the **SCM Agreement** because (1) the European Communities had contested the claims and arguments of Australia that the **SCM Agreement** has application to agricultural products and may apply to the same measures as are at issue pursuant to the **Agreement on Agriculture**; (2) the prohibitions in the **SCM Agreement** have no direct counterpart in the reduction commitment obligations in the **Agreement on Agriculture**; (3) the Appellate Body's decision in **Australia – Salmon** did not involve claims under the **SCM Agreement**, Article 4.7 of which imposes a duty on panels to recommend a time period for withdrawal of a measure; and (4) in the context of Article 19.2 of the **DSU**, a decision not to examine claims under the **SCM Agreement** would diminish the rights of Australia in regard to the implementation time period in the event of its claims proceeding. The European Communities opposed Australia's request. The Panel has modified paragraph 7.382 and has added paragraph 7.385 in response to Australia's comments but declines to change its decision to exercise judicial economy in this case.

6.15 Australia also requested that the Panel reconsider its comments in paragraph 7.386. Although the Panel does not consider that changes to paragraph 7.386 are necessary, it observes that its comments should not be taken in any way as a criticism of the manner in which the parties argued a highly complex case under tight time constraints. The point is merely that the focus of the dispute was understandably on the **Agreement on Agriculture** and that this was an additional consideration relevant to the Panel's judgement to exercise judicial economy in this case.
VII. FINDINGS

A. MAIN CLAIMS AND GENERAL ARGUMENTS OF THE PARTIES

7.1 The Complainants' claim\(^{346}\) that the European Communities has, since 1995, been exporting quantities of subsidized sugar in excess of its annual commitment levels, contrary to Articles 3 and 8 of the Agreement on Agriculture. In particular the Complainants claim that in the 2001-2002 marketing year the European Communities exported 4.097 million tonnes of subsidized sugar, well above the 1.273 million tonnes specified in its Schedule.\(^{347}\) The Complainants argue that, regardless of how the sugar is categorized, such subsidized exports of sugar were inconsistent with the European Communities' obligations under Articles 3, 8 and 9, or in the alternative, with Article 10.1 of the Agreement on Agriculture. Finally, the Complainants also claim that the said measures are inconsistent with the SCM Agreement.

7.2 The European Communities admits that its exports of sugar have been in excess of the figure shown in Section II, Part IV of its Schedule.\(^{348}\) The European Communities submits that its export subsidy commitments for sugar are, in fact, made up of two components: (i) one component which has been subject to progressive reduction during the implementation period; and (ii) a second component, Footnote 1 to Section II, Part IV to its Schedule containing the so-called "ACP/India sugar Footnote" which, it maintains, is subject to a ceiling of 1.6 million tonnes.\(^{349}\) Thus, for the European Communities, its exports of ACP/India equivalent sugar are not in excess of its commitment level. The European Communities denies that C sugar benefits from subsidies that are inconsistent with the Agreement on Agriculture or the SCM Agreement. The European Communities argues, "subsidiarily", that if the Panel concludes that C sugar is subsidized, the only course of action consistent with the requirement of good faith would be for the Complainants to agree to the correction of the European Communities' Schedule, in accordance with the Modalities Paper when interpreted in light of the principle of good faith.\(^{350}\) The European Communities rejects the Complainants' claims under Article 10.1 of the Agreement on Agriculture on the grounds that they are outside the Panel's terms of reference. In the alternative, the European Communities submits that exports of C sugar do not benefit from any "other export subsidies" within the meaning of Article 10.1. Finally, the European Communities contests the applicability of the SCM Agreement to the present dispute.

B. PROCEDURAL ISSUES IN THIS DISPUTE

1. The European Communities' challenges of the Panel's jurisdiction under its terms of reference

7.3 The Panel recalls the parties' arguments with respect to the terms of reference, summarized in paragraphs 4.10-4.24 above. The European Communities has raised various objections to the Panel's jurisdiction over some of the Complainants' claims under the Agreement on Agriculture. The European Communities submitted that the Complainants' panel requests did not include some of the claims they subsequently developed in their written and oral submissions. The European Communities also alleged that the Complainants have not always properly identified the measures subject to challenge.

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\(^{346}\) See the Complainants' panel requests in Annex D. The Panel also recalls that the complainants have accepted as their own the evidence and arguments submitted by the other complaining parties.

\(^{347}\) See para. 4.28 above.

\(^{348}\) European Communities' reply to Panel question No. 9.

\(^{349}\) See also paras. 4.191-4.193 above.

\(^{350}\) European Communities' first written submission, paras. 34, 142 and 192.
7.4 The Panel notes that pursuant to Article 7 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), the mandate and jurisdiction of a panel are determined by the complaint of the complaining parties which must comply with the requirements of Article 6 of the DSU. Pursuant to Article 6.1 of the DSU, the establishment of a panel by the Dispute Settlement Body (DSB) is quasi-automatic and a panel request is normally not subjected to detailed scrutiny by the DSB. It is therefore “incumbent upon a panel to examine the request for the establishment of the panel very carefully to ensure its compliance with both the letter and the spirit of Article 6.2 of the DSU.”

(a) The timing of objections to the Panel's jurisdiction

7.5 In the present dispute, the European Communities is not requesting any preliminary rulings within the meaning of paragraph 13 of the Panel’s Working Procedures. Yet, Australia alleges that the European Communities refrained from raising these issues until the time of its first written submission, some six months after the Panel was established and more than two months after the Panel was composed. Australia notes that the European Communities did not raise any concerns about the terms of reference at the time of Panel establishment; nor did it attempt to seek a preliminary ruling at an early stage of the Panel process (which it has done in other recent disputes in which it was a respondent).

7.6 The WTO jurisprudence is clear that parties should bring alleged procedural deficiencies to the attention of the other party and the Panel at the earliest possible opportunity. Conversely, the responding Members are required to seasonably and promptly bring claimed procedural deficiencies to the attention of the complaining Member and to the DSB or to the Panel, so that corrections, if needed, can be made in order that the dispute can be resolved. The Panel recalls that the procedural rules of WTO dispute settlement are designed to promote, not the development of litigation techniques, but the fair, prompt and effective resolution of trade disputes. In Mexico – Corn Syrup (Article 21.5 – US) the Appellate Body went as far as saying that "a Member that fails to raise its objections in a timely manner, notwithstanding one or more opportunities to do so, may be deemed to have waived its right to have a panel consider such objections.”

7.7 The Panel also recalls that when assessing any procedural objection, the Panel should "take into account whether the ability of the respondent to defend itself was prejudiced, given the actual course of the panel proceedings ...”

7.8 The Panel notes that although the European Communities asserted orally at the first and second meetings of the Panel that it had sustained prejudice, it offered no supporting particulars in its replies to the Panel's questions, in its submission or at the hearings.

352 Paragraph 13 of the Panel's Working Procedures: "A party shall submit any request for a preliminary ruling not later than in its first submission to the Panel. If the complaining party requests such a ruling, the respondent shall submit its response to the request in its first submission. If the respondent requests such a ruling, the complaining party shall submit its response to the request prior to the first substantive meeting of the Panel, at a time to be determined by the Panel in light of the request. Exceptions to this procedure will be granted upon a showing of good cause.”
354 See the Appellate Body Report on US – FSC, para. 166.
7.9 At the same time, the Panel agrees that certain issues relating to the "jurisdiction" of a panel can be raised at any time and even by the panel itself:

"[I]n the interests of due process, parties should bring alleged procedural deficiencies to the attention of a panel at the earliest possible opportunity. 358 (...) At the same time, however, as we have observed previously, certain issues going to the jurisdiction of a panel are so fundamental that they may be considered at any stage in a proceeding. 359 (emphasis added)"

7.10 The Panel is not convinced that the European Communities raised all its objections at the earliest possible time. Nevertheless, some of the European Communities' objections are concerned with the jurisdiction of this Panel, for which deficiencies cannot be cured. These objections may thus be viewed as so fundamental that they could be considered at any stage of the Panel proceeding. In this event, it is not clear to what extent the challenging Member needs to prove any prejudice. 360

7.11 In light of the above rules and with the view to ensuring clarity in the Panel's terms of reference and the security of this panel process, the Panel turns to exploring the issues of this Panel's jurisdiction and the European Communities' challenges thereof. 361

(b) The Complainants' requests for establishment of a panel 362

7.12 Before examining the parties' argumentation on the European Communities' objections to the Panel's jurisdiction under its terms of reference, the Panel recalls the relevant parts of the panel requests where the Complainants identified the measures at issue and the violations claimed to have occurred.

7.13 For Australia, the measures are:

(a) "The measures that are the subject of this request are the subsidies provided by the EC in excess of its reduction commitment levels on sugar and sugar containing products including sugar cane and sugar beet, processed and unprocessed cane and beet sugar and chemically pure sucrose in solid form, molasses resulting from the extraction of refining of sugar, isoglucose, inulin syrup and the other products listed in Article 1 of Council Regulation (EC) No 1260/2001 of 19 June 2001 on the European Communities' Common Organization of the markets in the sugar sector (Official Journal of the European Communities, 30 June 2001, L178/1-45).

The above mentioned subsidies are accorded through the EC sugar regime, which is contained in a number of EC regulations including Council Regulation No 1260/2001 and related EC regulations, administrative policies, rules, decisions and other instruments including instruments pre-dating the above regulation, and their

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362 The Complainants' panel requests are attached in Annex D below.
implementation. These various instruments will be referred to as “the EC sugar regime.”

and the violations are:

(b) "Australia considers that the provision of the above subsidies and the relevant elements of the EC sugar regime are inconsistent with the EC’s obligations under the following provisions: Articles 3.3, 8, 9.1(a), 9.1(c), and alternatively, 10.1 of the Agreement on Agriculture;"

in particular Australia adds:

"Australia is particularly concerned at the subsidies provided by the EC for ’C sugar’ exports under the EC sugar regime. Under the regime, producers of C sugar are able to sell C sugar on the world market at below the total average cost of production through cross-subsidisation of C sugar from quota sugar profits. By financing payments on the export of C sugar, the EC exceeds its export subsidy reduction commitments under the WTO Agreement on Agriculture.

Australia is also particularly concerned at the provisions of the EC sugar regime which accord direct subsidies contingent on export performance for quantities of approximately 1.6 million tonnes of sugar which are additional to the budgetary outlays and quantities of subsidised exports notified by the EC to the Committee on Agriculture under the provisions of Article 18.2 of the Agreement on Agriculture. In the application of those provisions, the EC significantly exceeds its budgetary outlays and quantity commitments for export subsidies on sugar under the Agreement on Agriculture."

7.14 For Brazil, the measures are:

(a) "The specific measures at issue in this dispute are the subsidies provided and maintained by the European Communities, in excess of the EC’s reduction commitment levels for sugar, under Council Regulation (EC) No. 1260/2001 of 19 June 2001 on the European Communities’ common organization of the markets in the sugar sector, and pursuant to all other legislation, regulations, administrative policies and other instruments relating to the EC regime for sugar, including the rules adopted pursuant to the procedure referred to in Article 42(2) of Council Regulation (EC) No. 1260/2001 of 19 June 2001, and any other provision related thereto."

and the violations are:

(b) "The EC provides export subsidies for sugar in excess of its reduction commitment levels specified in Section II of Part IV of its Schedule of Concessions (Schedule CXL-European Communities), in violation of the Agreement on Agriculture and the

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363 Australia’s panel request continues as follows: “In addition to setting down the conditions attaching to imports of sugar, the EC sugar regime provides conditions attached to the production, supply and exports of sugar, including domestic support and export subsidies. Sugar is classified into quota and non-quota sugar. Non-quota sugar is known as C sugar. The sugar regime provides for the reclassification from quota to C sugar and from C sugar to quota sugar. Sugar classified as C sugar cannot be disposed of in the EC market.”

364 See Australia’s panel request in Annex D below.

SCM Agreement. In particular, Brazil is concerned with two categories of subsidized EC exports:

(i) The EC sugar regime guarantees a high price for the sugar that is produced within production quotas. This is termed "A and B sugar". Sugar produced in excess of these quotas is termed "C sugar". Sugar classified as C sugar cannot be sold internally in the year in which it is produced, and must, in principle, be exported. Payments in the form of high prices provided to growers and processors by the EC sugar regime finance the production and export of C sugar at prices below its total cost of production.

(ii) The EC grants export subsidies to an amount of white sugar ostensibly equivalent to the quantity of raw sugar that the EC imports under its preferential arrangements. This amount, reportedly, is approximately 1.6 million tons.

The EC unjustifiably excludes these subsidies from the calculation of the total amount of export subsidies that it provides for sugar. The amount of sugar thus subsidized, alone or in combination with other export subsidies for sugar provided by the European Communities, exceeds the export subsidy reduction commitment levels and, as such, constitutes a violation of the EC's obligations under Articles 3.3, 8, 9.1 (a) and (c), or, alternatively, Article 10.1 of the Agreement on Agriculture ...

7.15 For Thailand the measures are:

(a) "The measures at issue are the export subsidies for sugar and sugar-containing products accorded under Council Regulation (EC) No. 1260/2001 of 19 June 2001 on the common organization of the markets in the sugar sector published in the Official Journal of the European Communities on 30 June 2001 (L 178/1-45) and related legal instruments."

and the violations are:

(b) "Under the EC sugar regime, sugar that is produced within production quotas ("A" and "B" quotas) is guaranteed a high intervention price. Sugar produced in excess of those quotas ("C-sugar") must in principle be exported. By virtue of the EC sugar regime, exporters of C-sugar are able to export such sugar at prices below the average cost of production. The EC therefore accords export subsidies to C-sugar in the form of payments on the export of sugar financed by virtue of governmental action. Furthermore, under its sugar regime, the EC grants export refunds to an amount of white sugar that the EC claims to be equivalent to the quantity of raw sugar imported under preferential import arrangements. The export refunds cover the difference between the world market price and the high prices in the EC for the products in question, thus making it possible for those products to be exported. The export refunds constitute direct subsidies contingent on export performance. Under the Agreement on Agriculture, the EC undertook budgetary outlay and export quantity reduction commitments with respect to sugar. In determining its budgetary outlays for export subsidies for sugar and the quantities benefiting from such subsidies, the EC does not take into account exports of C-sugar and exports of an

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366 See Brazil's panel request in Annex D below.
amount of white sugar equivalent to the quantity of raw sugar imported under preferential import arrangements.

As a result, the EC provides export subsidies for sugar in excess of its reduction commitments and consequently acts inconsistently with its obligations under Articles 3.3, 8, 9.1(a) and 9.1(c) of the Agreement on Agriculture or, alternatively, Article 10.1 of the Agreement on Agriculture. By granting export subsidies within the meaning of Articles 1.1(a)(1)(i) and (iv), 1.1(a)(2), and 1.1(b) of the SCM Agreement, that are not permitted by the Agreement on Agriculture, the EC also acts inconsistently with its obligations under Articles 3.1(a) and 3.2 of the SCM Agreement.

In sum, for Australia and Brazil the measures are the "subsidies in excess of the EC's reduction commitment levels under Council Regulation No. 1260/2001", while for Thailand the measures are the "export subsidies accorded under Council Regulation No. 1260/2001" on sugar. The violations claimed by the Complainants are essentially the same, that is that the European Communities is providing export subsidies for sugar in excess of its commitment level and consequently the European Communities is acting inconsistently with its obligations under Articles 3.3, 8, 9.1(a) and 9.1(c) of the Agreement on Agriculture or, alternatively, Article 10.1 of the Agreement on Agriculture.

In the Panel's view, although the Complainants drafted their panel requests using slightly different terms, each of the complaining parties' panel request has identified essentially the same measures – subsidies accorded under Council Regulation 1260/2001 for the EC sugar regime - and the same alleged violation – that the European Communities exceeds its budgetary outlays and quantity commitments contrary to Article 3 and 8 of the Agreement on Agriculture.

(c) Alleged lack of proper identification of the "measures" covered by the claims under Article 10.1 of the Agreement on Agriculture

In its first submission, the European Communities objected to the Complainants' claims under Article 10.1 of the Agreement on Agriculture, arguing that they are outside the Panel's terms of reference. In light of the Panel's decision in paragraph 7.357 hereafter to exercise judicial economy with respect to the Complainants' claims under Article 10.1 of the Agreement on Agriculture, there is no need for the Panel to assess that particular objection of the European Communities to the Panel's terms of reference.

(d) Alleged lack of proper identification of "payments" as distinct measures or distinct claims under Articles 3, 8 (and 9.1(c)) of the Agreement on Agriculture

(i) Arguments of the parties

The European Communities argued that the Complainants had not properly identified the measures that were inconsistent with the Agreement on Agriculture. The European Communities contended that the measures that allegedly violated Articles 3.3 and 8 of the Agreement on Agriculture were not the "export of sugar" as such, but the export subsidies granted by the European Communities. According to the European Communities, the Complainants should have identified, in their panel requests, the specific measures of the European Communities' sugar regime which, in their view, provided the alleged export subsidies applied by the European Communities in order to circumvent its reduction commitments. A simple reference to the European Communities' "sugar regime" or to Council Regulation No. 1260/2001 (which comprises of 51 articles, 6 annexes, and

367 See Thailand's panel request in Annex D below.

368 The Complainants also claim inconsistencies with the SCM Agreement, but these are not concerned by the European Communities' objections.
covers 45 pages of the Official Journal of the European Communities) was not considered to be sufficiently "specific" by the European Communities. Moreover, the European Communities held that the "exports of sugar" was a private transaction, not a government "measure", within the meaning of Article 6.2 of the DSU, and thus could not be the subject of dispute settlement.\textsuperscript{369}

7.19 The Complainants countered that they had sufficiently identified the regulations that were relevant in the present dispute at various stages in these proceedings and which resulted in excess production of subsidized sugar contrary to the European Communities' commitments. They considered the reference to EC Regulation No. 1260/2001 to be sufficiently specific to meet due process requirements. Brazil underlined that while it was theoretically possible that some subsections of EC Regulation No. 1260/2001 played no role in the provision of the challenged subsidies, Brazil's failure to identify and expressly exclude any of those subsections from its description of the measures at issue did not mean that Brazil had failed to identify those measures within the meaning of Article 6.2 of the DSU.

7.20 The European Communities argued that Brazil's "claims" regarding two forms of alleged payments i.e. those: (i) from EC consumers to EC sugar producers in the form of "artificially high" domestic prices for A and B sugar; and, (ii) payments-in-kind from the beet growers to the sugar producers in the form of C beet at prices below the minimum prices for A and B beet, had not been properly stated in Brazil's panel request.\textsuperscript{370} In support of its allegation, the European Communities referred to the Appellate Body report in \textit{Canada – Dairy} where it is stated that "[t]he second part of the claim is therefore, that the responding Member must have granted export subsidies with respect to quantities exceeding the quantity commitment level. There is, in other words a quantitative aspect and an export subsidization aspect to the claim."\textsuperscript{371} (emphasis added)

7.21 The European Communities submitted that Article 10.3 of the Agreement on Agriculture transfers the burden of proof only with respect to the "export subsidization aspect" of the Complainants' claim to the defending party. However, the European Communities argued, before such a transfer of the burden of proof can take place, it is necessary for the Complainants to state this as part of their claims. For the European Communities, Brazil's panel request failed to "provide a brief summary of the legal basis" that is "sufficient to present the problem clearly": Brazil's panel request mentioned only one of the "payments" further developed in its argumentation. For the European Communities, Brazil made no suggestion that there may be other "payments" which may also pose a "problem", let alone explain how such a "problem" would arise. For the European Communities, it remained unclear what precisely the other "payments" alleged by Brazil were, as, according to the European Communities, the description kept on changing.

7.22 The Complainants refuted the European Communities' assertion that their panel requests only covered certain forms of "payments".\textsuperscript{372} In Brazil's opinion, the existence of payments was only one aspect of the subsidies at issue in the present dispute.\textsuperscript{373} Brazil held that complaining Members are not required, by Article 6.2 of the DSU, to present evidence in their panel requests showing how and why exports of sugar are subsidized. They are only required to specify the measure at issue and the treaty provisions violated. Evidence has to be provided in their first written submissions.\textsuperscript{374}

\begin{footnotesize}
\begin{itemize}
\item\textsuperscript{369} See also paras. 4.10-4.13 above.
\item\textsuperscript{370} See European Communities' reply to Panel question No. 4; European Communities' second submission, paras. 5-6.
\item\textsuperscript{371} Appellate Body Report on \textit{Canada – Dairy (Article 21.5 – New Zealand and US II)}, para. 70.
\item\textsuperscript{372} Australia's second oral statement, para. 85.
\item\textsuperscript{373} Brazil's second oral statement, paras. 22-25.
\item\textsuperscript{374} Australia's second oral statement, para. 85; Brazil's second oral statement, paras. 22-25.
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The Complainants also held that, because of the reversal of the burden of proof, it was not incumbent on them to identify or enumerate the WTO agreements, provisions, or export subsidy definitions, that the European Communities might choose to invoke in its defence. It was the European Communities’ duty to prove that no subsidy of any kind, under any WTO agreement, had been granted by any EC measure to sugar exports in excess of its reduction commitments.

(ii) **Assessment by the Panel**

The Panel recalls the content of the Complainants’ Panel requests in paragraph 7.13, 7.14 and 7.15 and in Annex D to this Panel Report where the complaining parties have identified essentially the same measures and the same alleged violations (thus the same claims).

In the Panel’s view, the Complainants’ allegation that exports of C sugar, subsidized through the operation of EC Regulation No. 1260/2001, are in excess of the European Communities’ scheduled commitments and, thus, contravene Articles 3 and 8 of the Agreement on Agriculture, is sufficiently specific so as to allow the European Communities and the third parties to be "informed of the legal basis of the complaints".

The European Communities argued that the Complainants have confused the requirements of Article 6.2 of the DSU with respect to the specificity of panel requests and the consequences of the special rules on the burden of proof of Article 10.3 of the Agreement on Agriculture. Conversely, the Complainants submitted that it is the European Communities that has confused claims and arguments. The Panel examines these issues in turn.

In this dispute, the special rules on the reversal of the burden of proof of Article 10.3 of the Agreement on Agriculture have been invoked by the Complainants. Article 10.3 provides:

"Any Member which claims that any quantity exported in excess of a reduction commitment level is not subsidized must establish that no export subsidy, whether listed in Article 9 or not, has been granted in respect of the quantity of exports in question."

With respect to the issue of burden of proof and the special rule of Article 10.3, the Appellate Body in Canada – Dairy (Article 21.5 – New Zealand and US II) determined that there are two separate parts to a claim under Article 3 of the Agreement on Agriculture and in light of Article 10.3, a different standard of burden of proof applies to each part.

"In identifying the nature of the special rule, it is useful to analyze the character of claims brought under these provisions. Pursuant to Article 3 of the Agreement on Agriculture, a Member is entitled to grant export subsidies within the limits of the reduction commitment specified in its Schedule. Where a Member claims that another Member has acted inconsistently with Article 3.3 by granting export subsidies in excess of a quantity commitment level, there are two separate parts to the claim. First, the responding Member must have exported an agricultural product in quantities exceeding its quantity commitment level. If the quantities exported do

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375 Brazil's first oral statement, para. 51; Brazil's second written submission, paras. 7-15; Australia's reply to Panel question No. 4.
376 Ibid.
378 (footnote original) Under Articles 3.1 and 3.3 of the Agreement on Agriculture, "commitments limiting subsidization" of exports are specified in the Schedule in terms of "budgetary outlay and quantity commitment levels".
not reach the quantity commitment level, there can be no violation of that commitment, under Article 3.3. However, merely exporting a product in quantities that exceed the quantity commitment level is not inconsistent with the commitment. The commitment is an undertaking to limit the quantity of exports that may be subsidized and not a commitment to restrict the volume or quantity of exports as such. The second part of the claim is, therefore, that the responding Member must have granted export subsidies with respect to quantities exceeding the quantity commitment level. There is, in other words, a quantitative aspect and an export subsidization aspect to the claim. 

7.29 Therefore, the Panel is of the view that a claim under Article 3 of the Agreement on Agriculture requires allegations that, first, the European Communities has exported sugar above its commitment level and, second, that such exports of sugar were subsidized.

7.30 In the Panel's view, the Complainants have satisfied these requirements adequately. The legal basis of the Complainants' claims is Articles 3 and 8 of the Agreement on Agriculture. In their requests for establishment of a panel, the Complainants did not have to detail how and why such exports were being subsidized, only that the commitment levels were exceeded and that exports were subsidized. Moreover, the Complainants did indicate some aspects of the export subsidization of EC sugar in their panel requests (in referring to Article 9.1(a) and 9.1(c) of the Agreement on Agriculture).

7.31 Contrary to claims, which must be specifically identified in a panel request, parties' arguments can evolve and develop throughout the proceedings. In advance of the European Communities' response to their allegations, and to the extent that the European Communities would deny any subsidization of its exports of sugar, the Complainants developed in their first written submissions, arguments on why and how, in their view, exports of sugar were indeed subsidized. They did this in the attempt to further substantiate their claims that the European Communities was subsidizing exports of sugar in excess of its commitment level.

7.32 While the issue of the specificity of a panel request under Article 6.2 of the DSU can be determined on the face of the panel request, the issue of the burden of proof relates to the

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380 In EC – Bananas III, at para. 141, the Appellate Body held that "claims" which are to be outlined in a panel's request for the establishment of a panel are to be distinguished from "arguments" which are to be addressed at a later stage: "In our view, there is a significant difference between the claims identified in the request for the establishment of a Panel, which establish the Panel's terms of reference under Article 7 of the DSU, and the arguments supporting those claims, which are set out and progressively clarified in the first written submissions, the rebuttal submissions and the first and second Panel meetings with the parties". See also at para. 143: "Article 6.2 of the DSU requires that the claims, but not the arguments, must all be specified sufficiently in the request for the establishment of a Panel in order to allow the defending party and any third parties to know the legal basis of the complaint". (underlining added) See also the Appellate Body report on EC-Hormones, para. 156.

381 In US – Carbon Steel the Appellate Body stated, in para. 127: "As we have said previously, compliance with the requirements of Article 6.2 must be demonstrated on the face of the request for the establishment of a panel. Defects in the request for the establishment of a panel cannot be "cured" in the subsequent submissions of the parties during the panel proceedings. Nevertheless, in considering the sufficiency of a panel request, submissions and statements made during the course of the panel proceedings, in particular the first written submission of the complaining party, may be consulted in order to confirm the meaning of the words used in the panel request and as part of the assessment of whether the ability of the respondent to defend itself was prejudiced. Moreover, compliance with the requirements of Article 6.2 must be determined on the merits of each case, having considered the panel request as a whole, and in the light of attendant circumstances." (footnotes omitted) (emphasis added).
 substantive demonstrations of violations (through evidence and argumentation) taking place during the entire panel process.\textsuperscript{382}

7.33 Again in Canada – Dairy (Article 21.5 – New Zealand and US II), the Appellate Body determined that a different standard of burden of proof applies to each part of a claim under Article 3:

"Under the usual rules on burden of proof, the complaining Member would bear the burden of proving both parts of the claim. However, Article 10.3 of the Agreement on Agriculture partially alters the usual rules. The provision cleaves the complaining Member's claim in two, allocating to different parties the burden of proof with respect to the two parts of the claim we have described.

Consistent with the usual rules on burden of proof, it is for the complaining Member to prove the first part of the claim, namely that the responding Member has exported an agricultural product in quantities that exceed the responding Member's quantity commitment level\textsuperscript{383} (underlining added)

7.34 If the complaining Member succeeds in proving the quantitative part of the claim, and the responding Member contests the export subsidization aspect of the claim, then, under Article 10.3, the responding Member 'must establish that no export subsidy … has been granted' in respect of the excess quantity exported. (emphasis added) The language of Article 10.3 is clearly intended to alter the generally-accepted rules on burden of proof.\textsuperscript{384} While the Complainants bear the burden of proving that the export quantities are above the specific commitment level, once they have done so, it is for the European Communities to prove that such exports of sugar were not subsidized.

7.35 In the Panel's view, the Complainants' panel requests sufficiently informed the European Communities what measures the Complainants were challenging and what violations were claimed. This is obviously the case since in its first submission the European Communities stated that if the Panel considers that exports of C sugar are subsidized, the Panel should assess the situation in light of what the European Communities' commitment level should have been, had C sugar been calculated in accordance with the Modalities Paper.\textsuperscript{385} In the Panel's view, the Complainants' panel requests were sufficiently detailed "to present the problem clearly".\textsuperscript{386}

7.36 Therefore, the Panel considered that the Complainants' panel requests complied with the requirements of Article 6.2 of the DSU in that they adequately identified the measures at issue and the violations claimed to have occurred, i.e. that the European Communities' exports of subsidized sugar exceeded the European Communities' commitment level contrary to Articles 3 and 8 of the Agreement on Agriculture.

7.37 Consequently, the Complainants' argumentation that C sugar receives advantages from various subsidies and payments, within the meaning of Article 9.1(c) of the Agreement on Agriculture, is not outside the Panel's terms of reference.

\textsuperscript{382} Panel Report on Thailand – H-Beams, at para. 7.43.
\textsuperscript{385} European Communities' first written submission, para. 34.
\textsuperscript{386} Appellate Body Report on Korea – Dairy, para. 120.
(e) Alleged lack of proper identification of "claims" under Article 9.2(b)(iv) of the Agreement on Agriculture

(i) Arguments of the parties

7.38 The European Communities also contended that Article 9.2(b)(iv) of the Agreement on Agriculture was not mentioned in the Complainants' panel requests, nor in their first written submissions, (only in the first oral statements of Brazil and Thailand).\(^{387}\) The European Communities alleged that it had no idea, prior to the first substantive meeting, that the Complainants were claiming that Footnote 1 to Schedule the European Schedule CXL was also inconsistent with Article 9.2(b)(iv) of the Agreement on Agriculture.\(^{388}\) Accordingly, even if found to be acting inconsistently with Article 9.2(b)(iv) of the Agreement on Agriculture, the European Communities contended that this provision could not form the basis for a finding of inconsistency with any other provision of the Agreement on Agriculture. Moreover, the European Communities believed that the claim that its export subsidies had not been reduced sufficiently, though still unfounded, is quite different, from the qualitative point-of-view, from the claim that the European Communities had exceeded its export subsidy commitment levels.

7.39 The Complainants explained that Article 9.2(b)(iv) of the Agreement on Agriculture was introduced by them as a counter-argument and in response to arguments made by the European Communities, and not as a claim of violation requiring specification in their panel requests.\(^{389}\) The Complainants referred specifically to Article 9.2(b)(iv) of the Agreement on Agriculture to underline that accepting the Footnote to the European Communities' Schedule as valid, even if interpreted as imposing a quantity limit, led the European Communities to act inconsistently with its reduction obligations. As a consequence, the European Communities was providing export subsidies in a manner inconsistent with the Agreement on Agriculture – particularly in violation of Articles 3 and 8 of the Agreement on Agriculture.

(ii) Assessment by the Panel

7.40 As noted by the Panel before, the Complainants' main claim under the Agreement on Agriculture is that the EC sugar exports are being subsidized above the European Communities' commitment level in violation of Articles 3 and 8 of the Agreement on Agriculture. In the context of the parties' arguments and attempts to identify the relevant commitment level for the European Communities for sugar, the Complainants made reference to the provisions of Article 9.2(b)(iv) of the Agreement on Agriculture, which determines the Members' overall level of commitment at the end of the annual reduction stages of the implementation period. All parties agree that Members' commitment levels today are the same as they were at the end of the implementation period. Therefore, Brazil and Thailand made references to Article 9.2(b)(iv) of the Agreement on Agriculture as part of the legal context of Articles 3, 8 and 10.3 of the Agreement on Agriculture with a view to discussing the European Communities' commitment levels for exports of sugar since 2001, and in support of their argument that that commitment levels should be determined with reference to the European Communities' entries in Section II, Part IV of its Schedule.

7.41 The Panel recalls the distinction between claims and arguments.\(^{390}\) In the Panel's view, a panel request containing a claim under Article 3 of the Agreement on Agriculture must state that: (i)

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\(^{387}\) European Communities' first written submission, paras. 69-70; European Communities' reply to Panel question No. 28. See also para. 4.19 above.

\(^{388}\) European Communities' reply to Panel question No. 28.

\(^{389}\) Brazil's second oral statement, paras. 82-83. See also para. 4.18 above.

\(^{390}\) See the Appellate Body Reports on EC – Bananas III, paras. 142-143, EC – Hormones, para. 156, US – Certain EC Products, para. 123.
exports of the scheduled products are above commitment levels and (ii) such exports have been subsidized. In the Panel's view, the Complainants' panel requests comply with these requirements.\textsuperscript{391} Subsequently, during the panel process the Complainants were entitled to further develop their argumentation that the exceeding exports of sugar had benefited from export subsidies within the meaning of the \textit{Agreement on Agriculture}.

7.42 The European Communities submitted that "an appropriate test for distinguishing 'claims' from 'arguments' would be to anticipate what would be the consequences of upholding a given 'argument'. If upholding a purported 'argument' leads to establishing a violation of a legal provision, but does not render unnecessary the examination of another purported 'argument' made under the same legal provision, it is because each of the two 'arguments' involve a distinct 'claim'."\textsuperscript{392} The European Communities added that when this test is applied in the present case, it becomes clear that each of the "payments" alleged by Brazil is a distinct "claim".

7.43 The Panel does not agree with the European Communities' suggestion. The Panel is of the view that the European Communities' assertions are contrary to the existing WTO jurisprudence and to the Panel's discretion to reach a conclusion that a claim of violation is justified on the basis of arguments not even raised by the parties and, in certain situations, without having to address all the arguments of the parties. The Panel has already reached the conclusion that the Complainants have adequately identified the measures at issue and the related violations of the \textit{Agreement on Agriculture}.

7.44 In the Panel's view, the European Communities' allegation that the Complainants' arguments and references to Article 9.2(b)(iv) are outside the Panel's terms of reference is thus not founded.

(f) Alleged lack of proper identification of claims in relation to Footnote 1 to the EC's Schedule (ACP/India sugar)\textsuperscript{393}

(i) Arguments of the parties

7.45 In its first submission, the European Communities also observed that the Complainants had made subsidiary claims that the European Communities was not respecting the terms of Footnote 1 to its Schedule. The European Communities considered that these claims were not sufficiently identified. The European Communities therefore argued that it could not defend any (unidentified) measure which it may have adopted with respect to ACP/India sugar in respect of unidentified provisions of the \textit{Agreement on Agriculture}, or provisions which were merely cited without further explanation. The European Communities contended that these claims were not made in the requests for establishment of a panel by the Complainants, which allege an "exclusion" or a failure to "take into account" exports of ACP/India equivalent sugar in ensuring respect of the European Communities' export subsidy commitments, and not a failure to respect the terms of the Footnote. Consequently, for the European Communities, these claims were also outside the terms of reference of the Panel

7.46 The Complainants were of the view that the European Communities was confusing Footnote 1 with "the measure at issue" and was attempting to redefine the measure at issue as

\textsuperscript{391} See the Appellate Body Report in \textit{Korea – Dairy} in para. 120: "(...) The request must: (i) be in writing; (ii) indicate whether consultations were held; (iii) identify the specific measures at issue; and (iv) provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly. In its fourth requirement, Article 6.2 demands only a summary – and it may be a brief one – of the legal basis of the complaint; but the summary must, in any event, be one that is sufficient to present the problem clearly’. It is not enough, in other words, that ‘the legal basis of the complaint’ is summarily identified; the identification must ‘present the problem clearly’.”

\textsuperscript{392} European Communities' reply to Panel question No. 4.

\textsuperscript{393} Footnote 1 to Section II, Part IV of the EC's Schedule is hereafter called the "Footnote 1" or the "ACP/India sugar Footnote", the precise content of which is discussed in paras. 7.167-7.196 hereafter.
Footnote 1 itself. Nowhere in their panel requests did the Complainants cite Footnote 1 as being a "measure at issue". Rather, the European Communities was informed by the Complainants' panel requests that the exports in excess of reduction commitments arose from the subsidized export of C sugar and ACP/India equivalent sugar. Australia noted that the European Communities' first written submission deliberately avoided claims of inconsistency arising from the export subsidies granted to ACP/India equivalent sugar. Instead, the European Communities had redefined the measure as the Footnote, and referred exclusively to Footnote 1 in relation to ACP/India equivalent sugar. Australia added that in the fourth and fifth paragraphs of its panel request, Australia identified the measures at issue as the subsidies on sugar in excess of the European Communities' reduction commitments and elaborates on the nature of the measures in paragraphs 6-7 of that request.

7.47 According to the Complainants, the European Communities is using Footnote 1 as a rebuttal argument to the Complainants' claims of inconsistency. The Complainants added that it is perfectly in order for any complainant to anticipate such an argument in its first written submission or to respond to such arguments in its rebuttal submission. Such issues are not connected to Article 6.2 of the DSU and to the requests for establishment of a panel. Finally, the Complainants reiterated that the European Communities is confusing "claims", which must be made in the panel request, and "arguments", which are developed during the panel proceeding. The Complainants claimed that the European Communities exceeds its subsidy reduction commitments, inter alia, by granting export subsidies to ACP/India equivalent sugar. The Complainants argued that Footnote 1 does not exempt the European Communities from its obligations under Articles 3.3, 8, 9.1(a) and 9.1(c) of the Agreement on Agriculture or, alternatively, that it does not apply to the exports of a quantity of EC sugar that is equivalent to the quantity of sugar imported from the ACP countries and India. The Complainants' argument regarding the scope of application of Footnote 1 is thus a subsidiary argument supporting their legal claims that the European Communities is exceeding its export subsidy reduction commitments.

(ii) Assessment by the Panel

7.48 The Panel recalls the content of the Complainants' panel requests and the distinction between claims and arguments. The Complainants' claim is that the European Communities is exporting sugar (C sugar and ACP/India equivalent sugar) in excess of the European Communities' commitment level. For the Complainants, the European Communities' commitment level is indicated in Section II, Part IV of the EC Schedule for sugar, that is 1,273,500 tonnes in 2001 and the following years.

7.49 In the Panel's view, the European Communities is using Footnote 1 as a rebuttal argument to the Complainants' claims that the European Communities is acting inconsistently with Articles 3 and 8 of the Agreement on Agriculture. The European Communities is arguing that its level of commitment includes an additional 1.6 million tonnes of ACP/India equivalent sugar as provided for in Footnote 1.

7.50 In the Panel's view, what constitutes a Member's "commitment level", for the purpose of Article 10.3, is both an issue of legal interpretation and a matter of evidence. Whether or not an entry in a Member's schedule, such as the European Communities' Footnote 1, could compose part of that Member's overall commitment level is a legal issue for which both sides have submitted argumentation. It is for the Panel to decide whether the "commitment level" referred to in Articles 3, 8, 9.2(b)(iv) and 10.3 is exclusively composed of the export subsidies that had to be reduced (in the case of the EC sugar 1,273,500 tonnes) or whether Members are also entitled to maintain, for instance, ad hoc "limitations" on export subsidization.

7.51 The European Communities argues that a correct interpretation of Articles 3, 8 and 9 of the Agreement on Agriculture and the European Communities' Footnote 1 would lead to the conclusion
that the European Communities' Footnote 1 is a component of its overall export subsidy commitments. The Complainants disagree.

7.52 In the Panel's view, when the European Communities made reference to Footnote 1 as evidence and in support of its argument that its level of commitment was not limited to 1,273,500 tonnes but, rather, should include the 1.6 million tonnes mentioned in Footnote 1, the Complainants had the right to challenge such arguments as well as the scope of the European Communities' commitment; the Complainants were entitled to use rebuttal arguments to challenge the conclusions drawn by the European Communities from Footnote 1. Again the Panel recalls that the Complainants' claims are not that the EC's Schedule contains a WTO inconsistent entry (Footnote 1) or that the European Communities' categorization of its subsidies is inconsistent with the Agreement on Agriculture but rather that the European Communities is exporting subsidized sugar in quantities above the European Communities' scheduled commitment levels specified in Section II, Part IV of its Schedule. The Panel additionally notes that in their panel requests the three complaining parties mentioned the issue of subsidies to exports of products either as "equivalent to the quantity of raw sugar imported under preferential arrangements", or for quantities of approximately 1.6 million tonnes of sugar which are additional to the budgetary outlays and quantities of subsidised exports notified by the EC to the Committee on Agriculture thereby putting the European Communities on notice of the legal and factual matters at issue.

7.53 For the foregoing reasons, the Panel is of the view that the Complainants' argumentation with respect to the scope of the European Communities' commitment levels, including those relating to the nature, legal effect and scope of the European Communities' Footnote 1, is within the Panel's terms of reference.

2. European Communities' allegation that the Complainants are "estopped" from pursuing this dispute

(a) Arguments of the parties

7.54 The Panel refers to Section IV:D.3 of the descriptive part for a summary of the parties' arguments in respect to good faith and estoppel. The European Communities submits that the violations now alleged by the Complainants would have been flagrant and immediately manifest upon the conclusion of the WTO Agreement. Yet, none of the Complainants raised any question with respect to exports of C sugar until this dispute. This is interpreted by the European Communities to mean that, for many years after the conclusion of the WTO Agreement, the Complainants continued to share the European Communities' understanding that exports of C sugar were not subsidized. The same is true with respect to issues relating to the ACP/India sugar Footnote which have never been raised in the Committee on Agriculture and have never previously been challenged by the Complainants.

7.55 For the European Communities, the Complainants' silence may be legitimately construed as a representation of lack of objections not only where there is a "duty to speak", but also in circumstances where it is reasonable to expect that the other parties will speak. For the European Communities, it was reasonable to expect that Members would not challenge the fact that it did not include the additional subsidies of the ACP/India sugar Footnote and C sugar in its base quantity. On the basis of what it considers to be its good faith expectations, the European Communities submits that the Complainants are estopped from bringing this claim.

394 See Brazil and Thailand's 'Panel requests in Annex D to this Panel Report.
395 See Australia's Panel request in Annex D to this Panel report.
396 See European Communities' first written submission, para. 139.
7.56 The European Communities argues that estoppel is a procedural defence, which precludes one party from exercising a right vis-a-vis another party, but without modifying the substantive obligations of that party. It adds that estoppel is a matter of adjectival, rather than substantive, law and accordingly the effect of a true estoppel is confined to the parties. The European Communities does not contend that its obligations under Article 9.1(c) of the Agreement on Agriculture have been modified by virtue of the principle of estoppel. Rather, the European Communities' contention is that the Complainants are precluded from bringing a claim under that provision and, therefore, that the Panel should reject their claims even if it upheld them in substance.

7.57 For the European Communities, since estoppel does not alter the substantive rights of Members under the WTO Agreement, but only the exercise of those rights, it may operate exclusively between two Members. 397

7.58 The Complainants respond that, as a matter of legal principle, the European Communities could not infer from silence that other Members shared the view that C-sugar was not subsidized, because they did not have a "duty" to object. The Complainants submit that even if they had been silent, their silence on the European Communities' base quantity levels as well as the ACP/India sugar Footnote does not amount to a clear and unambiguous representation upon which the European Communities could rely, especially as there was no legal duty upon the Complainants to do so. 398

7.59 For Australia, if the European Communities were permitted to have recourse to estoppel, it would operate to diminish the rights of the Complainants, contrary to the provisions of Articles 3.2 and 19.2 of the DSU. It is one thing to have a right subject to relevant provisions of a covered agreement, but entirely another to have that right subject to the operation of a principle which is not recognized in the provisions of the covered agreement. Furthermore, Australia argues that it is the responsibility of the European Communities to make sure it is acting in accordance with the Agreement on Agriculture and other WTO Agreements.

7.60 Finally, the Complainants argue that even if estoppel could be invoked, the European Communities does not comply with the basic requirements for invoking estoppel. 399

(b) Assessment by the Panel

7.61 The Panel notes that parties and third-parties to this dispute do not seem to agree on the nature of the principle on estoppel and its exact parameters. 400 Muller and Cottier define it as follows:

"It is generally agreed that the party invoking estoppel 'must have been induced to undertake legally relevant action or abstain from it by relying in good faith upon clear and unambiguous representations by the other State'." 401

7.62 The Black Law Dictionary defines "silence, estoppel by" as follows:

"Such estoppel arises where person is under duty to another to speak or failure to speak is inconsistent with honest dealings. Silence, to work 'estoppel', must amount

\[\text{References:}
397 \text{See also paras. 4.167-4.170 above.}
398 \text{See also paras. 4.160-4.161 above.}
399 \text{See para. 4.159}
400 \text{Australia's second submission, paras. 142 and 144; Brazil's second submission, Title G and paras. 80 and 85; Thailand's second submission, para. 114; EC's first submission, paras. 136-138; and see for example: United States oral statement, paras. 8-9; Colombia's oral statement, para. 8; ACP countries' third party submission, paras. 9 and 126; and ACP countries' oral statement, para. 8.}
401 \text{J.P. Müller and T. Cottier, in Encyclopaedia of Public International Law, Ed. Max Planck Institute, North Holland, 1992, p. 116.}
to bad faith, and, elements or essentials of such estoppel include: change of position to prejudice of person claiming estoppel; damages if the estoppel is denied; duty and opportunity to speak; inducing person claiming estoppel to alter his position; knowledge of facts and of rights by person estopped; misleading of party claiming estoppel; reliance upon silence of party sought to be estopped.”

7.63 In the Panel’s view, it is far from clear whether the principle of estoppel is applicable to disputes between WTO Members in relation to their WTO rights and obligations. The principle of estoppel has never been applied by any panel or the Appellate Body. Estoppel is not mentioned in the DSU or anywhere in the WTO Agreement.

7.64 If estoppel, as a general principle of law, were applicable to disputes between WTO Members, Members would still have to comply with the DSU and would thus have to find a way to comply in good faith with both the provisions of the DSU and those of estoppel. The Panel recalls that in EC – Hormones, the Appellate Body made clear that even if there were a precautionary principle in general international law, WTO obligations remained binding on Members: “We accordingly agree with the finding of the Panel that the precautionary principle does not override the provisions of Articles 5.1 and 5.2 of the SPS Agreement.”

7.65 If estoppel were considered as a customary rule of interpretation or if it were comprised in the good faith principle reflected in Article 3.10 of the DSU, such a principle would have to be read “harmoniously” with the other principles of the WTO dispute settlement system, including the quasi-automaticity of its process and the fact that the initiation of the dispute settlement mechanism is self-regulating. On several occasions, the Appellate Body has insisted that it is "the duty of any treaty interpreter to read all applicable provisions of a treaty in a way that gives meaning to all of them, harmoniously".

7.66 The Panel also recalls that the Appellate Body has clearly established that initiation of WTO dispute settlement procedures does not require the demonstration of any specific legal or economic interest. In Mexico – Corn Syrup (Article 21.5 – US) the Appellate Body ruled that the first sentence of Article 3.7 of the DSU:

”... reflects a basic principle that Members should have recourse to WTO dispute settlement in good faith, and not frivolously set in motion the procedures contemplated in the DSU. We recall that, when we examined the language of Article 3.7 of the DSU in our Report in European Communities – Bananas, we stated that:

‘... a Member has broad discretion in deciding whether to bring a case against another Member under the DSU. The language of Article XXIII:1 of the GATT 1994 and of Article 3.7 of the DSU suggests, furthermore, that a Member is expected to be largely self-

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7.67 Given the "largely self-regulating" nature of the requirement in the first sentence of Article 3.7, panels and the Appellate Body must presume, whenever a Member submits a request for establishment of a panel, that such a Member does so in good faith, having duly exercised its judgement as to whether or not recourse to that panel would be "fruitful".

Given the "largely self-regulating" nature of the requirement in the first sentence of Article 3.7, panels and the Appellate Body must presume, whenever a Member submits a request for establishment of a panel, that such a Member does so in good faith, having duly exercised its judgement as to whether or not recourse to that panel would be "fruitful".

7.68 This is in line with GATT jurisprudence on this matter. In the GATT dispute on EEC – Import Restrictions, the panel concluded that:

"The Panel ... recognized that restrictions had been in existence for a long time without Article XXIII ever having been invoked by Hong Kong with respect to the products concerned, but concluded that this did not alter the obligations which contracting parties had accepted under GATT provisions. Furthermore the Panel considered it would be erroneous to interpret the fact that a measure had not been subject to Article XXIII over a number of years, as tantamount to its tacit acceptance by contracting parties ...." (emphasis added)

7.69 In the Panel's view, Article 3.7 of the DSU neither requires nor authorizes a panel to look behind that Member's decision or to question its exercise of judgement (unless there is evidence of bad faith). Under WTO jurisprudence, the fact that a Member does not complain about a measure at a given point in time, cannot by itself deprive that Member of its right to initiate a dispute at some later point in time if that Member considers in good faith that it is fruitful to do so. This seems to be confirmed by the WTO dispute cases such as in EC – Bananas III (Article 21.5 – EC/Ecuador) and in Guatemala – Cement II.

7.70 Moreover, assuming arguendo that estoppel could be invoked in WTO dispute settlement proceedings, the Panel is of the view that the present situation is not one for which estoppel could find application. The Panel examines hereafter the requirements for its application.

7.71 The conditions for estoppel have been summed up by the panel in Argentina – Poultry:

"[T]he essential elements of estoppel are: '(i) a statement of fact which is clear and unambiguous; (ii) this statement must be voluntary, unconditional, and authorized; (iii) there must be reliance in good faith upon the statement ... to the advantage of the party making the statement'."

7.72 In Guatemala – Cement II, the panel considered that:

"[E]stoppel is premised on the view that where one party has been induced to act in reliance on the assurances of another party, in such a way that it would be prejudiced were the other party later to change its position, such a change in position is 'estopped', that is precluded."
In the Panel's view, Brazil's and Thailand's silence concerning the European Communities' base quantity levels as well as with respect to the ACP/India sugar Footnote does not amount to a clear and unambiguous representation upon which the European Communities could rely, especially considering that, in the Panel's view, there was no legal duty upon the Complainants to alert the European Communities to its alleged violations. Furthermore, it is not possible to identify any facts or statements made by the Complainants where they have admitted that the EC measure was WTO consistent or where they have promised that they would not take legal action against the European Communities. In the Panel's view the "silence" of some of the Complainants cannot be equated with their consent to the European Communities' violations, if any. Moreover, the Complainants' silence cannot be held against other WTO Members who, today, could decide to initiate WTO dispute settlement proceedings against the European Communities. In other words, even if the three Complainants had remained completely silent on this issue, their silence could not be considered a commitment binding on other Members to the extent that it would contradict the provisions of the Agreement on Agriculture or which could remove the European Communities' alleged inconsistencies with its WTO obligations.

The Appellate Body has clearly established that WTO Members must comply with their WTO obligations in good faith and that the WTO Agreement must be interpreted in good faith. In the Panel's view both the European Communities and the Complainants have acted in good faith in the initiation and conduct of the present dispute proceedings. The European Communities is entitled to defend its sugar regime and has done so. The Complainants were entitled to initiate the present WTO proceedings as they did and at no point in time have they been estopped, through their actions or silence, from challenging the EC sugar regime which they consider WTO inconsistent.

In the Panel's view, if it were to conclude that the Complainants are now estopped from challenging the EC sugar regime or its alleged excessive export production of subsidized sugar, the Panel would be acting contrary to Articles 3.2 and 19.2 of the DSU which provide that panels and the Appellate Body are prohibited from adding to or diminishing Members' rights and obligations.

3. The *amicus curiae* of WVZ

(a) Factual background

As referred to in paragraph 2.20 above, on 24 May 2004, the Panel received an unsolicited "amicus curiae" brief from the Wirtschaftliche Vereinigung Zucker (hereafter "WVZ"), the association of German sugar producers and beet growers, which submitted that C sugar does not benefit from export subsidies, in essence, because the European Communities' intervention price does not cover the average total cost of producing A, B and C sugar, in the European Communities.

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416 Article 3.2 of the DSU is as follows: "The dispute settlement system of the WTO is a central element in providing security and predictability to the multilateral trading system. The Members recognize that it serves to preserve the rights and obligations of Members under the covered agreements, and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law. Recommendations and rulings of the DSB cannot add to or diminish the rights and obligations provided in the covered agreements." Article 19.2 of the DSU is as follows: "In accordance with paragraph 2 of Article 3, in their findings and recommendations, the panel and Appellate Body cannot add to or diminish the rights and obligations provided in the covered agreements." See also the Appellate Body Report on India – Patents (US), paras. 46-47.
7.77 Following the recommendation of the Appellate Body in *US – Shrimp* in the context of *amicus curiae* briefs that "the exercise of the panel's discretion could, of course, and perhaps should, include consultation with the parties to the dispute"\(^{417}\), and with a view to ensuring due process, the Panel invited the parties on 27 May 2004 to make comments on the *amicus curiae* brief of WVZ by 1 June 2004.\(^{418}\)

7.78 The Complainants requested in their comments that the Panel reject the document submitted by WVZ on the grounds of inaccuracy of the facts and analysis advanced by WVZ, late timing of the document and due process considerations, and they further contended that this submission addressed issues that have already been argued at length by the parties. In its third communication relating to the *amicus curiae* brief, Brazil claimed that there was evidence that a breach of confidentiality had occurred (the Panel discusses the issue of the breach of confidentiality in the following section of the Panel Report). The European Communities informed the Panel that it did not wish to provide comments.

7.79 In their comments on the amicus brief, the Complainants challenged in detail the allegations made by WVZ as being utterly unfounded, *inter alia* because producers received much more than the intervention price and because the calculations made by WVZ were not based on accurate data or the proper interpretation of the data.

(b) Assessment by the Panel

7.80 First, the Panel wishes to recall that it does not consider that *amicus curiae* briefs can be taken into account in a manner that would circumvent the parties' rights and obligations under the *DSU*, the *Agreement on Agriculture* and the *WTO Agreement* generally.\(^{419}\)

7.81 The Panel notes that the WVZ submission was filed almost two weeks after the Panel's second meeting with the parties. The Panel, as other panels before, considers that the timing of the *amicus curiae* submission plays an important role in the acceptance or rejection of *amicus curiae* briefs.\(^{420}\) In this regard Thailand argued that in accordance with the Working Procedures of the Panel proceedings, no new arguments or evidence were to be submitted by the parties after the second meeting. However, the Panel recalls that at the end of the second meeting the Panel asked additional legal and factual questions of the parties and the Complainants requested that they be entitled to comment on each other's replies to the Panel's questions. The period within which the Panel could receive new arguments and evidence was therefore extended until Wednesday, 2 June 2004. However, WVZ comments are not related to the Panel's questions or the parties' comments.

7.82 The Panel has decided not to consider further the *amicus curiae* from WVZ because, *inter alia*, it is based on confidential information and is thus evidence of a breach of confidentiality which disqualifies the credibility of the authors. Brazil informed every authorized recipient of its submission

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\(^{418}\) This position of the Appellate Body would seem to be supported by Article 12.1 of the *DSU* providing that panels need to consult the parties when they decide to add or deviate from the Working Procedures in Appendix 3 of the *DSU*. Appendix 3 of the *DSU* is silent regarding *amicus curiae* briefs. Appellate Body Report on *US – Shrimp*, para. 105.

\(^{419}\) The Appellate Body determined in *Japan – Agricultural Products II*, that expert advice could be taken into account but that it did not relieve the complaining party of making a prima facie case of inconsistency. See Appellate Body Report on *Japan – Agricultural Products II*, para. 129.

\(^{420}\) See Panel Report on *US – Softwood Lumber III*, where the panel rejected three unsolicited *amicus curiae* briefs because they were presented after the first substantive meeting, Panel Report on *US – Softwood Lumber III*, para. 7.2; and Panel Report on *US – Lead and Bismuth II*, where the panel chose not to accept the submission because it had been submitted too late and could have unjustifiably delayed the proceedings; Panel Report on *US – Lead and Bismuth II*, para. 6.3.
of the confidential nature of the latter. On 10 June 2004, the Panel therefore requested WVZ to identify the source of the information used in its *amicus curiae* brief. WVZ acknowledged that it "was able to examine" Brazil's exhibit but refused to provide the source of its information: "WVZ is not in a position to reveal the source of its information regarding the evidence submitted by Brazil."

7.83 The Panel regrets this refusal to cooperate which, regardless of the merits (or lack thereof) of WVZ submission, undermines not only elemental fairness to the parties, but also compromises the integrity of the dispute settlement system itself by hindering further openness and the transparency of the dispute settlement process.

7.84 The WTO dispute resolution confidentiality rules apply to WTO Members, the Panel members and WTO staff involved in the dispute proceedings. Nevertheless, the Panel considers that if the WVZ, though not a party to the proceedings, wanted to be considered a "friend of the court", it should have followed an appropriate standard of behaviour towards the Panel and the parties together with making every possible effort to respect WTO dispute settlement rules, including confidentiality rules.

7.85 In light of the above, the Panel, having the discretionary legal authority to accept and consider or not unsolicited *amicus curiae* briefs submitted by individuals or organizations, whether governmental or non-governmental,⁴²¹ declares to further consider the *amicus curiae* brief submitted by WVZ.

4. Breach of confidentiality

(a) Factual background⁴²²

7.86 Brazil informed the Panel on 2 June 2004 that the *amicus curiae* brief submitted by WVZ, the association of German sugar producers, disclosed information that Brazil had submitted to the Panel in confidence. Brazil, accordingly, wished to bring the alleged breach of confidentiality to the Panel's attention and requested that the Panel "investigate how the breach occurred" and that it take any further action that it deems appropriate, including "mak[ing] a full report of this incident to the Dispute Settlement Body." Thailand and Australia supported the comments and request made by Brazil in this regard.

7.87 The Panel noted in a letter to the parties and third parties, dated 4 June 2004, the seriousness of the matter at issue, and invited them to comment on Brazil's allegation, and on the appropriate remedy, "if such a breach had in fact occurred". Such comments were to be submitted by 8 June 2004. The Panel received responses within this timeframe from Australia, Thailand, the European Communities (parties), and from India (third party).

7.88 The European Communities noted that it attached the utmost importance to the strict observance by all parties and third parties of the confidentiality rules set out in the DSU and in the Working Procedures of the Panel. It shared the concerns expressed by Brazil, and noted for the record that it had treated as strictly confidential all information designated as such in these proceedings.

7.89 Australia observed that the cost of production data cited by WVZ was also included in a confidential exhibit submitted by Australia⁴²³ and requested that the Panel undertake an investigation of the source of the LMC information cited by WVZ. Australia submitted that in the event that the

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⁴²¹ Appellate Body Reports on *US – Shrimp*, para. 107 and on *US – Lead and Bismuth II*, para. 41.
⁴²² See paras. 2.21 to 2.28 above.
⁴²³ The WVZ quoted LMC figure of costs of production of ***/tonne which is cited in table 2 of Exhibit ALA-1, p. 8.
Panel establishes a breach of confidentiality on the part of any party to this dispute, specifically in reference to the LMC data designated as confidential by Brazil and Australia, that the Panel record the breach of confidentiality in its report, in the context of Article 3.10 of the DSU. Australia further considered that any unauthorized use or citation of information which has been designated as confidential by a party to a dispute should automatically constitute grounds for rejection of an amicus submission.

7.90 Thailand supported the comments and requests made by Brazil and Australia.

7.91 On 10 June 2004, the Panel, by letter, requested information from WVZ "with respect to the exact source[s] (documents, websites, etc.) used for the data referred to” in its document and a clarification as to the use of the euro currency in such data.

7.92 The Panel received a response from WVZ on 15 June 2004 in which WVZ indicated that it had been "able to examine" an attachment to Brazil's submission. According to WVZ, this document was not designated as confidential. It also indicated that WVZ was "not in a position to reveal the source of its information regarding the evidence submitted by Brazil." It did not discuss the currency of such data.

7.93 Comments on the response from WVZ were received from Brazil on 18 June 2004 in which Brazil reiterated its request that the Panel summarily reject the WVZ amicus brief and report the incident to the Dispute Settlement Body. Furthermore, Brazil submitted that the cover and every page of all hard copies of the exhibit in question provided to the Panel, the parties and third parties, were stamped manually, in block letters, "CONFIDENTIAL". Brazil had stated in its cover letters, that its submissions, including its two exhibits, were confidential. The recipients of electronic copies were also put on notice as to the confidential nature of all its submissions. Every authorized recipient of Brazil's submission was thus made aware of the confidential nature of the documents.

7.94 Brazil also submitted that it had, to the best of its knowledge, confirmed with LMC, that the total cost of production figures referred to in the amicus curiae brief of WVZ appear only in the LMC report commissioned by Brazil which, again, were submitted to the Panel as a confidential document in one of its exhibits. Moreover, Brazil noted that the data referred to by WVZ in its amicus curiae brief do not appear in the December 2003 report referred to in WVZ's footnote 2, or in any other LMC report, which had been made available to the public.

(b) Assessment by the Panel

7.95 On the issue of confidentiality, the Panel recalls that, in addition to its emphasis on the confidentiality of Members' oral and written submissions to the panels and the Appellate Body, Article 18.2 of the DSU provides explicitly that Members must respect the confidentiality of any information designated as such by another Member in the context of the settlement of a dispute:

"Written submissions to the panel or the Appellate Body shall be treated as confidential, but shall be made available to the parties to the dispute. Nothing in this Understanding shall preclude a party to a dispute from disclosing statements of its own positions to the public. Members shall treat as confidential information submitted by another Member to the panel or the Appellate Body which that Member has designated as confidential... ."

7.96 The Panel recalls that the Complainants had explicitly designated the said LMC Report as confidential. The Panel also wishes to recall that on a number of occasions throughout the proceedings of this Panel it strongly emphasized and reminded parties and third parties of the confidential nature of the DSU proceedings.
This is not the first time that an amicus curiae brief, submitted in the context of a WTO dispute settlement proceeding, has contained confidential information. In Thailand – H-Beams, an industry association submitted an amicus curiae brief which cited Thailand's confidential submission. The Appellate Body on the basis of its own examination of the facts believed that there was prima facie evidence that the association received, or had access to, the appellant's submission in that appeal and saw no reason to accept the written brief submitted. The Appellate Body returned the brief to its sender.\textsuperscript{424} Other breaches of confidentiality have also been reported.\textsuperscript{425}

The Panel has come to the conclusion that a breach of confidentiality did occur in the framework of these proceedings. The Panel is therefore concerned and deeply deplores this breach of confidentiality and the disregard of a requirement imposed by the DSU and the Panel's Working Procedures. The Panel considers that it has used its best endeavours to investigate the alleged breach of confidentiality. However, the Panel has not been able to determine the source of the breach.

The Panel hereby reports the incident to the Dispute Settlement Body.

Having examined the procedural issues relevant to the present dispute, the Panel now proceeds to examine the Complainants' substantive claims.

C. ORDER OF ANALYSIS BY THE PANEL

In light of Article 21.1 of the Agreement on Agriculture, Article 3 of the SCM Agreement\textsuperscript{426} and the relevant jurisprudence, the Panel shall first examine the consistency of the challenged export subsidies on sugar, an agricultural product, first under the Agreement on Agriculture\textsuperscript{427} as the Complainants have argued their claims under the Agreement on Agriculture first.

The Complainants have submitted that the European Communities is exporting subsidized sugar in excess of its commitment levels contrary to Articles 3, 8, and 9 of the Agreement on Agriculture. The parties disagree as to what constitutes the European Communities' commitment level. While the Complainants argue that the European Communities' quantity commitment level is to be determined with reference to its entry in Section II of Part IV of its Schedule, the European Communities submits that its commitment comprises two components: one component is its entry in Section II of Part IV of its Schedule and the other component includes the additional quantity of 1.6 million tonnes provided for in Footnote 1 (the ACP/India sugar Footnote) to Section II, Part IV of its Schedule. The Panel must thus determine, first, what constitutes the European Communities' commitment level for the purpose of Articles 3 and 8 of the Agreement on Agriculture.

Moreover, the determination of the European Communities' quantity commitment level is crucial to the operation of the special rule, provided for in Article 10.3 of the Agreement on Agriculture.
Agriculture, invoked by the Complainants. When Article 10.3 is invoked by a complaining Member, and it is proven that exports actually exceed the challenged Members’ commitment level, it is for that exporting Member to demonstrate that its exports are not subsidized. Based on the Panel's conclusions on the European Communities’ commitment level for sugar and the Panel's conclusions on the application of Article 10.3, the Panel will then proceed to assess whether the European Communities' exports of sugar exceed the European Communities' commitment level, inconsistently with Articles 3 and 8 of the Agreement on Agriculture.

7.104 In Section D.2 below, the Panel examines first whether the ACP/India sugar Footnote relating to 1.6 million tonnes of sugar can be considered as part of the European Communities' commitment level. In Section D.3, the Panel addresses the European Communities' argument that participants in the Uruguay Round (now Members of the WTO), have "agreed" to the inclusion of Footnote 1 in Section II of Part IV of the European Communities' Schedule. Finally, once the Panel has determined the European Communities' commitment level, it will be able, in Section E, to determine whether Article 10.3 of the Agreement on Agriculture can find application in the present dispute where the Complainants have claimed violations of Articles 3 and 8 of the Agreement on Agriculture. If this is the case, the Panel will examine whether the Complainants have made a prima facie factual demonstration of the quantitative aspect of their claims, namely that the European Communities has exported quantities of sugar in excess of its quantity commitment level; if it is so, the Panel will then determine whether the European Communities has demonstrated, pursuant to Article 10.3 of the Agreement on Agriculture, that its excess exports of sugar, are not subsidized.

7.105 The Panel recalls the factual description of the EC sugar regime in Section III above.

D. THE EUROPEAN COMMUNITIES' EXPORT SUBSIDY COMMITMENT LEVELS FOR SUBSIDIZED EXPORTS OF SUGAR

1. Introduction

7.106 The Complainants consider that the European Communities' commitment levels for subsidized exports of sugar are as specified in Section II of Part IV of the EC Schedule CXL 428, entitled:

"Part IV: AGRICULTURAL PRODUCTS: COMMITMENTS LIMITING SUBSIDISATION (Article 3 of the Agreement on Agriculture)

SECTION II: Export Subsidies : Budgetary Outlay and Quantity Reduction Commitments."

7.107 Under the line entitled "Sugar" for 2000, the following quantity is specified:

"1,273,500 tonnes"

Besides the term Sugar, a footnote (1) is inscribed and at the bottom of the page one can read:

"Does not include exports of sugar of ACP and Indian origin on which the Community is not making any reduction commitments. The average of export in the period 1986 to 1990 amounted to 1,6 mio t."

7.108 The Panel assesses hereafter what the commitment level of the European Communities is with respect to exports of sugar pursuant to Articles 3, 8 and 9 of the Agreement on Agriculture.

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428 See Annex C, also provided as Exhibit EC-1 and Exhibit COMP-16.
2. **What is the European Communities' commitment level in light of the ACP/India sugar Footnote?**

(a) Arguments of the parties

7.109 Further to their claims, the Complainants underline that, in every marketing year since 1995, the European Communities' total exports of sugar have consistently exceeded its scheduled commitment levels. In particular, during the marketing year 2001-2002, the European Communities exported 4.097 million tonnes of sugar which was well in excess of the European Communities' scheduled commitment level for that year, i.e. 1,273,500 tonnes.

7.110 In response, the European Communities submits that its level of reduction commitment is not 1,273,500 tonnes only. The European Communities argues that a correct interpretation of the Footnote leads to the conclusion that the Footnote is one of the two components of the European Communities' export subsidy commitments. For the European Communities, the first sentence confirms that exports of an "equivalent" amount of ACP/Indian sugar are not included in the quantities and outlays reported by the European Communities for the base period level (1986-1990) which served as a basis for the figures set out in the table. The second sentence, in the European Communities' view, expresses the "average of export" of ACP/India "equivalent" sugar in the base period 1986-1990. The second sentence is not a simple statement of fact or a narration of particular circumstances. Rather, the European Communities contends, it operates in precisely the same way as the other component of the European Communities' commitments: it is a ceiling, or limitation on subsidization, and a limited authorization to provide export subsidies.

7.111 Consequently, the European Communities submits that it has acted consistently with Article 8 of the Agreement on Agriculture since it has provided subsidies only in conformity with the Agreement on Agriculture and with the commitments as specified in its schedule. Further, the European Communities considers that it has respected the commitments it has undertaken to limit subsidization on A and B sugar and ACP/India "equivalent" sugar, and therefore, the European Communities has acted consistently with Article 3 of the Agreement on Agriculture. Moreover, since the European Communities has not provided export subsidies in excess of the commitment levels set out in its Schedule, it has acted consistently with Articles 3 and 8.432

7.112 The Complainants counter that all export subsidies under the Agreement on Agriculture are subject to reduction. The Complainants reason that, as sugar is a product "specified" in the European Communities' Schedule, the European Communities is under the obligation to reduce its budgetary outlays and subsidized sugar exports in accordance with its scheduled commitments. If Footnote 1 was part of the European Communities' export subsidy commitments, export subsidies provided for by the said Footnote should have been reduced.

7.113 On the other hand, the European Communities considers that, overall, its export subsidies on sugar have been reduced and it is therefore complying with Articles 3 and 8 of the Agreement on Agriculture. The European Communities also argues that Article 3.3 incorporated the export subsidy commitments into the GATT, but did not prescribe any form for such commitments. In Footnote 1 the commitment has taken the form of a limit on subsidization in the form of a ceiling level contained in a footnote to a Member's Schedule.

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429 See para. 7.106 above
430 See paras. 4.30-4.31 above.
431 See paras. 4.191-4.192 above.
432 See para. 4.193 above.
7.114 The Complainants submit that Members could not exempt themselves from their obligations under the Agreement on Agriculture by including reservations in their Schedule of Concessions that would subsequently be accorded the same, or greater weight, than any provision of a WTO Agreement with which the schedule text might directly conflict such as with the fundamental provisions of the Agreement on Agriculture. If the differences between the terms of a schedule and the terms of the Agreement on Agriculture cannot be reconciled by interpretation through Articles 31 and 32 of the Vienna Convention, a conflict exists. The Complainants submit that GATT and WTO jurisprudence endorsed by the Appellate Body establishes that WTO Members could incorporate in their Schedule of Concessions only acts yielding rights, not acts diminishing obligations. Therefore the Footnote was legally invalid. Moreover, to the extent that the European Communities purported to diminish its obligations under the Agreement on Agriculture, the Footnote, in their view, constituted an impermissible reservation under international law and WTO law.

7.115 With respect to the Complainants' alleged conflicts between the ACP/India sugar Footnote and Articles 3 and 8 of the Agreement on Agriculture, the European Communities responded that when properly interpreted, the Footnote could not be considered to conflict with the Agreement on Agriculture. For the European Communities, the Panel was not obliged to declare the Footnote, which was part of a validly concluded treaty, invalid. The European Communities notes that under general public international law, one part of a treaty could rarely render another part of the same treaty without legal effect.

7.116 Subsidiarily, the Complainants argue that the terms of the Footnote do not mean what the European Communities intends to draw from this Footnote. The Complainants submitted that the terms of the Footnote applied exclusively to imports of raw "sugar of ACP and Indian origin". The Footnote thus contemplates exclusively the re-export of sugar of ACP or Indian origin. Moreover, the Footnote does not mention, and could not be interpreted to cover, "equivalent" exports. Thus, even if the Panel were to find that Members could exempt themselves from their obligations under the Agreement on Agriculture by inserting footnotes in their Schedules of Concession, the Panel would have to conclude that the footnote inserted by the European Communities did not exempt it from those obligations in respect of the quantities of sugar equivalent to sugar of ACP and Indian origin.

7.117 The European Communities replied that it was well known to all parties at the time of conclusion of the WTO Agreement, that the European Communities did not grant export refunds on the re-export of sugar of ACP/Indian origin, but rather to a quantity equivalent to such imports. The European Communities had made its intentions clear in two letters, when submitting draft schedules and associated documents to all participants in the negotiation, reiterating its objective to have the footnote accepted by the other negotiating parties.

7.118 The European Communities argued that participants in the Uruguay Round could negotiate departures from the reduction formula agreed in the Modalities Paper, and that the Footnote constituted one such departure. For the European Communities, the Complainants had agreed to this Footnote during the Uruguay Round negotiations. In this context, the European Communities considered that, by virtue of Article 16 of the Vienna Convention, the Complainants had consented

\[433\) See para. 4.215 above.
\[434\) See also para. 4.215 above.
\[435\) See also para. 4.217 above.
\[436\] Article 16 of the Vienna Convention reads as follows:

"Exchange or deposit of instruments of ratification, acceptance, approval or accession

Unless the treaty otherwise provides, instruments of ratification, acceptance, approval or accession establish the consent of a State to be bound by a treaty upon:

(a) their exchange between the contracting States;"
to be bound by the terms of the treaty Footnote contained in the European Communities' Schedule, by ratifying the WTO Agreement.

7.119 The Complainants responded that they did not "agree" that this Footnote entitled the European Communities to export an additional 1.6 million tonnes of subsidized sugar. For the Complainants, even their alleged silence at the time of the conclusion of the Uruguay Round could not be considered to be an acceptance. They added that the European Communities cannot find anything in the Modalities Paper which would support its argumentation.

(b) Assessment by the Panel

(i) Introduction

7.120 In the present dispute, parties disagree on the European Communities' commitment level for exports of subsidized sugar. In light of the parties' arguments, the Panel needs to determine what can compose a Member's "commitment level" for the purpose of Article 3 of the Agreement on Agriculture in light of the European Communities' argument that its commitment is composed of its specific entry in Section II, Part IV of its Schedule (1,273,500 tonnes of sugar) as well as an additional 1.6 million tonnes relating to ACP/India sugar contained in Footnote 1 to the European Communities' Schedule. The Complainants claim that this Footnote reduces and contradicts, and thus conflicts with, the European Communities' fundamental obligations under the Agreement on Agriculture and as such does not modify the EC's commitment level specified in Section II, Part IV of the European Communities' Schedule.

7.121 In the Panel's view, what constitutes a Member's "reduction commitment level" for the purpose of Article 10.3 of the Agreement on Agriculture or the "reduction commitment within the meaning of Article 9 or the "commitment levels" within the meaning of Article 3.3 or the "commitment as specified in a Member's schedule" within the meaning of Article 8 of the Agreement on Agriculture is an issue of legal interpretation, for which there is no burden of proof as such. It is for the Panel to decide whether the "commitment levels" or the "reduction commitment levels" are (b) their deposit with the depositary; or (c) their notification to the contracting States or to the depositary, if so agreed."

437 The Panel recalls the Appellate Body's conclusion in EC – Hormones, para. 156, that "Panels are inhibited from addressing legal claims falling outside their terms of reference. However, nothing in the DSU limits the faculty of a panel freely to use arguments submitted by any of the parties - or to develop its own legal reasoning - to support its own findings and conclusions on the matter under its consideration. Recently in EC – Tariff Preferences, para. 105, the Appellate Body clarified that the burden of proof is relevant when dealing with "evidentiary" issues but not with "legal" interpretation. Therefore, it is always for the panel to provide the appropriate legal interpretation independently of what is put forward by any party.

"Consistent with the principle of jura novit curia it is not the responsibility of the European Communities to provide us with the legal interpretation to be given to a particular provision in the Enabling Clause; instead, the burden of the European Communities is to adduce sufficient evidence to substantiate its assertion that the Drug Arrangements comply with the requirements of the Enabling Clause." (footnotes omitted)

FNT 7: " The principle of jura novit curia has been articulated by the International Court of Justice as follows: It being the duty of the Court itself to ascertain and apply the relevant law in the given circumstances of the case, the burden of establishing or proving rules of international law cannot be imposed upon any of the parties, for the law lies within the judicial knowledge of the Court. (International Court of Justice, Merits, Case Concerning Military and Paramilitary Activities in and against Nicaragua (Nicaragua v. United States of America), 1986 ICJ Reports, p. 14, para. 29 (quoting International Court of Justice, Merits, Fisheries Jurisdiction Case (United Kingdom of Great Britain and Northern Ireland v. Iceland), 1974 ICJ Reports, p. 9, para. 17))"
composed exclusively of the commitments for export subsidies that have to be reduced (in the case of the EC sugar 1,273,500 tonnes) or whether Members are also entitled to maintain, for instance, ad hoc "limitations" on export subsidization not subject to reduction which would therefore be part of the overall commitment level of a Member.

7.122 To resolve the issue before it, the Panel will therefore have to examine the relationship between terms of (and commitments contained in) a Member's Schedule, in this dispute the content of Footnote 1 (on ACP/India sugar), and the provisions of the Agreement on Agriculture. In particular, the Panel needs to assess whether it is possible to interpret harmoniously the terms of the Agreement on Agriculture together with those of Footnote 1 of Section II, Part IV of the European Communities' Schedule. If this is not possible, the Panel will have to resolve such a conflict.

7.123 For the Panel to assess whether there is a conflict between Footnote 1 to Section II of Part IV of the European Communities' Schedule, and Articles 3, 8 and 9 of the Agreement on Agriculture, the Panel must first determine the extent and the scope of Members' obligations under those provisions. Second, the Panel will need to examine what Members are entitled to do in their Schedules and how terms of Members' Schedules should be interpreted. Thirdly, the Panel will examine the nature of the commitment, if any included in Footnote 1. The Panel will then discuss the relationship between the European Communities' obligations under Articles 3, 8 and 9 of the Agreement on Agriculture and Footnote 1 with a view to assessing whether the two sets of rights and obligations can be read harmoniously or whether they conflict. The Panel will then be able to conclude on the European Communities' commitment level for exports of sugar for the purposes of the present dispute.

(ii) The obligations of the Agreement on Agriculture with respect to export subsidies – Articles 3, 8 and 9 of the Agreement on Agriculture

7.124 In order to assess the Complainants' claims that the European Communities exceeded its level of commitments for exports of subsidized sugar, and the parties' disagreement on the European Communities' level of commitment for exports of subsidized sugar, the Panel interprets first the provisions of the Agreement on Agriculture dealing with Members' obligations with respect to exports subsidies on agricultural products.

7.125 The Panel notes first that Article 3 does not define the terms "commitment level", nor do Articles 9 and 10.3 of the Agreement on Agriculture define the term "reduction commitment" level. Moreover, Article 8 does not define what can constitute "commitments as specified in that Member's Schedule".

7.126 Since, pursuant to Article 31 of the Vienna Convention, the ordinary meaning of the terms do not inform the Panel sufficiently, the Panel proceeds to the examination of the "context" of Articles 3, 8, 9 and 10 of the Agreement on Agriculture, so as to allow the Panel to assess what can comprise a "Member's commitment level" for the purposes of Articles 3.3, or a Member's "specified commitment" within the meaning of Article 8 of the Agreement on Agriculture, and a Member's "reduction commitment" for the purpose of Articles 9 and 10.3 of the Agreement on Agriculture. The Panel thus examines Members' obligations with respect to export subsidies, as reflected in those provisions.

438 As a subsidiary argument, the Complainants have submitted that a good faith interpretation of Footnote 1 does not lead to the conclusion that the ACP/India sugar Footnote contains such a limitation or ceiling on subsidization. Australia's second written submission, paras. 161-162.

439 Article 31.1 and 31.2 of the Vienna Convention provide that: "A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose. 2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes (...)" The text of Articles 31, 32 and 33 of the Vienna Convention can be found in footnote 431 hereafter.
7.127 Article 8 of the *Agreement on Agriculture* on "Export Competition Commitments" contains a **general prohibition** on export subsidies and provides 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."

7.128 The commitments that are specified in Part IV, Section II, of a Member's Schedule describe for each product or group of products concerned, the maximum quantities in respect of which export subsidies, as defined in Article 1(e) of the *Agreement on Agriculture*, may be provided, as well as the associated maximum levels of budgetary outlays. These commitments are made an integral part of the GATT 1994 under Article 3.1 of the *Agreement on Agriculture*. The products which are subject to reduction commitments and in respect of which export subsidies may be used within the specified limits are commonly referred to as "scheduled products". Other products, not specified in Schedules, are referred to as "non-scheduled products".

7.129 The export subsidies listed in paragraph 1 of Article 9 of the *Agreement on Agriculture*, which had also served as the basis for establishing export subsidy reduction commitments in the Uruguay Round negotiations, are subject to the following **specific prohibitions** set out in Article 3.3 of the *Agreement on Agriculture*, the first of which relates to "scheduled products":

"Subject to the provisions of paragraphs 2(b) and 4 of Article 9, a Member shall not provide export subsidies listed in paragraph 1 of Article 9 in respect of the agricultural products or groups of products specified in Section II of Part IV of its Schedule in excess of the budgetary outlay and quantity commitment levels specified therein and shall not provide such subsidies in respect of any agricultural product not specified in that Section of its Schedule." (emphasis added)

7.130 It may also be noted that the first terms of Article 3.3 of the *Agreement on Agriculture* make clear that the final reduction commitment levels are binding beyond the end of the implementation period referred to in Articles 9.2 and 9.4 of the *Agreement on Agriculture*. Article 3.3 thus complements the provisions of Article 9.2.

7.131 The Panel notes also that Article 3.1 of the *Agreement on Agriculture* provides that "export subsidy commitments in Part IV of each Member's Schedule constitute commitments limiting subsidization." Article 3.3 of the *Agreement on Agriculture* requires that, with respect to agricultural products specified in Section II of Part IV of its schedule, "a Member shall not provide export subsidies … in excess of the budgetary outlay and quantity commitment levels specified therein." Article 3.3 of the *Agreement on Agriculture* makes clear that the commitments are those specified in a Members' Schedule.

7.132 Article 3.3 of the *Agreement on Agriculture* requires that the export subsidies listed in Article 9.1 of the *Agreement on Agriculture* can only be provided in accordance with a Member's Schedule. Therefore, a Member must not provide export subsidies on scheduled agricultural products beyond its budgetary and quantity commitment levels set out in its Schedule and shall not provide export subsidies on products not specified in its Schedule. As mentioned, Article 8 of the *Agreement on Agriculture* similarly provides that Members shall not "provide export subsidies otherwise than in conformity with this Agreement and with the commitments as specified in that Member's Schedule."

7.133 Article 9.1 of the *Agreement on Agriculture* describes **specific** types of export subsidies "subject to reduction commitments" and provides for schedules specifying commitments to reduce budgetary outlays for subsidies and quantities of exports receiving subsidies ("The following export subsidies are subject to reduction commitments under this Agreement"). The Panel also notes that
Section II of Part IV is entitled "Budgetary Outlay and Quantity Reduction Commitments." In the Panel's view, Article 9.1 of the Agreement on Agriculture makes clear that in the absence of a specific exemption contained in that Agreement, all export subsidies coming within the definitions of Article 9.1(a) – 9.1(f) have to be subject to reduction commitments. Specifically, in accordance with Article 9.2(b)(iv) of the Agreement on Agriculture, at the end of the implementation period, the Schedule must provide for budgetary outlay and quantity commitments no greater than 64 and 79 per cent of their respective base period levels. This is the case for Members who took advantage of the flexibility of Article 9.2(b) which was the case of the European Communities. Therefore, export subsidies contained in Section II, Part IV of a Member's Schedule ought to have been subject to the reduction commitments provided for in Article 9 of the Agreement on Agriculture.

7.134 In sum, in the Panel's view, Articles 8 and 3 of the Agreement on Agriculture make it clear that Members may not provide export subsidies other than in conformity with the Agreement on Agriculture and - not "or" - Members' Schedules. In particular, Article 3 of the Agreement on Agriculture provides that export subsidies are only possible for products listed in Section II, Part IV of Members' Schedules and only for amounts at or below the maximum level of commitment provided for in a Member's schedule. Through the application of Articles 3, 9.1 and 9.2(b)(iv) of the Agreement on Agriculture, all WTO-consistent export subsidies on scheduled products have been subject to reduction commitments.

7.135 The Panel notes also that Article 3.3 of the Agreement on Agriculture contemplates that a Member may exclude an agricultural product entirely from Part IV, Section II of its Schedule, but does not contemplate that when an agricultural product is included in its Schedule, subsidies provided to that product do not have to be reduced.

7.136 In the Panel's view, this is in line with the Preamble of the Agreement on Agriculture – as legal context to Articles 3, 8 and 9 – which in its third and fourth paragraphs provide:

"Recalling further that the above-mentioned long-term objective is to provide for substantial progressive reductions in agricultural support and protection sustained over an agreed period of time, resulting in correcting and preventing restrictions and distortions in world agricultural markets; Committed to achieving specific binding commitments in each of the following areas: market access; domestic support; export competition; and ..."

7.137 In the Panel's view, to comply with Article 3.3 of the Agreement on Agriculture, a Member that exports a scheduled product must comply with two distinct requirements: (1) its subsidized exports must be within the quantity limitation specified in its schedule; and (2) its corresponding budgetary outlays must also be within its commitments. The Panel considers that Article 3.3 (and Article 9.2(b)(iv)) makes it clear that the level of commitment of export subsidies on specified products must be scheduled both in terms of quantity and in terms of budgetary outlays, as the level of reduction of any such export subsidies apply to both their quantity and to their budgetary outlays: "a Member shall not provide export subsidies ... in excess of the budgetary outlay and quantity commitment levels specified [in its Schedule]." (emphasis added).

440 Article 9.2(f) of the Agreement on Agriculture provides that: "In any of the second through fifth years of the implementation period, a Member may provide export subsidies listed in paragraph 1 above in a given year in excess of the corresponding annual commitment levels in respect of the products or groups of products specified in Part IV of the Member's Schedule, provided that: (iv) the Member's budgetary outlays for export subsidies and the quantities benefiting from such subsidies, at the conclusion of the implementation period, are no greater than 64 per cent and 79 per cent of the 1986-1990 base period levels, respectively. For developing country Members these percentages shall be 76 and 86 per cent, respectively."

441 See G/AG/N/EEC/20/REV.1, dated 9 March 2000, at p. 2.
7.138 The European Communities counters that export subsidies do not have to be expressed both in terms of budgetary outlays and quantity. The Panel notes that if the EC's Schedule did not specify both of these limitations, it could export a subsidized scheduled product in excess of its commitment level and remain in compliance with Article 3.3 of the Agreement on Agriculture, because the challenging Member will be unable to demonstrate that the European Communities' exports do not exceed either of the two limitations. In the Panel's view, if Article 3.3 of the Agreement on Agriculture did not impose an obligation to have both a budgetary outlay and a quantity commitment level, then it would be effectively impossible, after the conclusion of the implementation period, to ensure that export subsidies never exceed the two levels set out in Article 9.2(b)(iv) of the Agreement on Agriculture which includes both.

7.139 For the European Communities the obligation to schedule both types of commitments was only set out in paragraph 11 of the Modalities Paper, from which, the Members could "negotiate departures". As evidence of such Members' practice, the European Communities suggests that Australia and New Zealand negotiated such departures from the Modalities Paper. Australia had sub-divided the category "other milk products" into two categories, fats and solid non-fats (which were not listed in the Modalities Paper), specifying separate quantity commitments, while indicating a budgetary outlay commitment only on the general product. New Zealand did not specify any quantitative limits but only scheduled reductions in budgetary outlays.

7.140 After examining Australia's Schedule, the Panel is of the view that Australia has scheduled both forms of reduction commitments, budgetary outlay as well as quantity, in respect of a single product group, i.e. "other milk products", benefiting its sub-category of fats and non-fats. Turning to New Zealand's Schedule, the Panel concludes that Members which have undertaken reduction commitments covering all Annex 1 products have scheduled both the budgetary outlay, and the

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442 European Communities' second written submission, para. 128. See also European Communities' reply to the Panel question No. 29.
443 And the European Communities add that Footnote 1 is a negotiated departure.
444 See the Modalities Paper, Exhibit EC-27.
445 The Panel considers that the product category "other milk products" has been subjected to a budgetary outlay commitment, while the volume of "other milk products" has been expressed in terms of its fat, and solid non fat, content prior to the scheduling of the corresponding quantity reduction commitment. While the quantity reduction commitments have been expressed taking account of fat content, the Panel considers that they relate to the same product group, i.e. "other milk products". The data and the explanatory notes contained in Supporting Table 11 of document G/AG/AGST/AUS support the Panel's view. Further, the manner in which these two forms of reduction commitments are integrated in the scheduling table, as well as in Supporting Table 11, leaves no doubt as to the Panel's conclusion that Australia has scheduled both forms of reduction commitments covering all Annex 1 products have scheduled both the budgetary outlay, and the

446 The Panel considers that an indication with respect to the quantity commitment level is not missing. Instead, it is specified as "not applicable" for all implementation years, except for the last year 2000, where the specified amount is clearly indicated as "0.00", thus implying a 100 per cent reduction of the volume of subsidized agricultural exports. Further, the reduction commitment relates, not to the individual product categories identified during the Uruguay Round, but to "all agricultural products described in Annex 1 of the Agreement on Agriculture". Quite apart from the fact that it may not be feasible, from the statistical point-of-view, to obtain a single figure expressing a quantity commitment level for all agricultural products, given the variety of measurement units and conversion factors involved, the Panel appreciates that the nature of the export incentive schemes reported by New Zealand during the base period did not lend itself to the breakdown required by the Modalities Paper. Seeking further guidance from the Schedule of the only other Member of the WTO, Panama, which has undertaken a reduction commitment in Section II of Part IV, on an aggregate basis, the Panel finds, again, that: (a) the products covered are "todos los productos descritos en el Anexo 1 del Acuerdo sobre la Agricultura"; and that (b) the quantity commitment level is shown as "no aplicable" except for the last implementation year, 2003, where the amount is clearly specified as "0".
quantity reduction commitments, in a consistent and uniform manner, by clearly specifying a figure with respect to the last implementation year.

7.141 In the Panel’s view, Australia’s and New Zealand’s scheduled reduction commitments cannot be assimilated to examples of “negotiated departures” from the Modalities Paper, as claimed by the European Communities.

7.142 On the basis of the evidence submitted to it, the Panel, therefore, concludes that the European Communities has not substantiated its assertion that there are other situations in which a Member has undertaken commitments in Section II of Part IV of its Schedule that did not contain both budgetary outlays and quantity commitment levels.

7.143 Therefore the Panel concludes that the Agreement on Agriculture makes it clear that export subsidies are only possible for products listed in Section II, Part IV of Members’ Schedules and only for amounts at or below the maximum level of commitment provided for in a Member’s Schedule. Moreover, all WTO-consistent export subsidies must have been specified in a Member’s Schedule, both in terms of quantity and in terms of budgetary outlays and all WTO-consistent export subsidies on scheduled products must have been subject to reduction commitments during the implementation period.

(iii) The interpretation of terms included in WTO Members’ Schedules

7.144 One of the issues before the Panel is whether the European Communities’ commitment level with respect to export subsidies on sugar can legally include two components: the first component being the commitment levels expressed in the table on export subsidies (which have decreased during the implementation period of the Agreement on Agriculture and has remained fixed since 2001); the second component being the commitment levels expressed in Footnote 1 to the EC’s Schedule in respect of ACP/India sugar. For the Complainants, Footnote 1 on ACP/India sugar is inconsistent with the Agreement on Agriculture and should be ignored when determining the European Communities’ commitment level.

7.145 In order for the Panel to determine the European Communities’ commitment level, the Panel must assess the legal value and effect of Footnote 1 contained in Section II of Part IV of the EC’s Schedule and to what extent the content of such a Footnote can legally modify the European Communities’ obligations under the Agreement on Agriculture with respect to export subsidies.\[447\] Before assessing the legal value and effect of Footnote 1, the Panel examines how one should interpret provisions contained in Members’ Schedules, in particular when such scheduled provisions seem to contradict basic obligations contained in a WTO multilateral trade agreement, such as the Agreement on Agriculture.

Provisions of a Member’s Schedule should be interpreted as treaty provisions

7.146 As mentioned above, Article 8 of the Agreement on Agriculture makes it clear that Members must respect both the provisions of the Agreement on Agriculture and the provisions of their Schedules. The Panel notes first that scheduled commitments are made an integral part of the GATT 1994 under Article 3.1 of the Agreement on Agriculture.

7.147 In EC – Computer Equipment, the Appellate Body concluded that provisions of a Member’s schedule must be interpreted as treaty provisions:

\[447\] The Panel notes first that none of the parties have argued that footnotes per se cannot contain commitments. The Complainants have raised objection to the content of Footnote 1 and the interpretation thereof provided by the European Communities.
"Tariff concessions provided for in a Member's Schedule -- the interpretation of which is at issue here -- are reciprocal and result from a mutually-advantageous negotiation between importing and exporting Members. A Schedule is made an integral part of the GATT 1994 by Article II:7 of the GATT 1994. Therefore, the concessions provided for in that Schedule are part of the terms of the treaty. As such, the only rules which may be applied in interpreting the meaning of a concession are the general rules of treaty interpretation set out in the Vienna Convention.\textsuperscript{448}

7.148 Therefore, provisions of a Members' Schedule must be interpreted pursuant to Article 3.2 of the DSU and Articles 31, 32 and 33 of the Vienna Convention.\textsuperscript{449}

\textsuperscript{448} Appellate Body Report on EC – Computer Equipment, para. 84.

\textsuperscript{449} Articles 31, 32 and 33 of the Vienna Convention read as follows:

"Article 31 – General rule of interpretation

1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.

2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes:

(a) any agreement relating to the treaty which was made between all the parties in connection with the conclusion of the treaty;

(b) any instrument which was made by one or more parties in connection with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

3. There shall be taken into account, together with the context:

(a) any subsequent agreement between the parties regarding the interpretation of the treaty or the application of its provisions;

(b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation;

(c) any relevant rules of international law applicable in the relations between the parties.

4. A special meaning shall be given to a term if it is established that the parties so intended.

Article 32 – Supplementary means of interpretation

Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31:

(a) leaves the meaning ambiguous or obscure; or

(b) leads to a result which is manifestly absurd or unreasonable.

Article 33 – Interpretation of treaties authenticated in two or more languages

1. When a treaty has been authenticated in two or more languages, the text is equally authoritative in each language, unless the treaty provides or the parties agree that, in case of divergence, a particular text shall prevail.
7.149 The primary purpose of treaty interpretation is to identify the common intention of the parties. Importantly, in EC – Computer Equipment, the Appellate Body clarified that although unilaterally proposed and bilaterally negotiated, tariff concessions still represent the common agreement of all Members and are thus multilateral obligations; it also concluded that "indeed, the fact that Members' Schedules are an integral part of the GATT 1994 indicates that, while each Schedule represents the tariff commitments made by one Member, they represent a common agreement among all Members." (underlining added)

7.150 The Panel believes that this is true for all WTO scheduled commitments, whether pure market access concessions or any other commitments. WTO Members' scheduled commitments, whether initially negotiated bilaterally or multilaterally, are multilateralized when made part of the WTO Agreement, and thus, they should be interpreted accordingly.

Effective treaty interpretation

7.151 The requirement that a treaty be interpreted in "good faith" pursuant to Article 31.1 of the Vienna Convention can be correlated with the principle of "effective treaty interpretation", according to which all terms of a treaty must be given a meaning. On several occasions, the Appellate Body has emphasized the importance of the principle of effectiveness whereby "an interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility".

7.152 In Korea – Dairy, the Appellate Body concluded that:

"In light of the interpretive principle of effectiveness, it is the duty of any treaty interpreter to 'read all applicable provisions of a treaty in a way that gives meaning to all of them, harmoniously.' An important corollary of this principle is that a treaty

2. A version of the treaty in a language other than one of those in which the text was authenticated shall be considered an authentic text only if the treaty so provides or the parties so agree.

3. The terms of the treaty are presumed to have the same meaning in each authentic text.

4. Except where a particular text prevails in accordance with paragraph 1, when a comparison of the authentic texts discloses a difference of meaning which the application of articles 31 and 32 does not remove, the meaning which best reconciles the texts, having regard to the object and purpose of the treaty, shall be adopted."


450 See the Appellate Body Report on US – Gasoline, at para. 23. See also the Appellate Body Reports on Japan – Alcoholic Beverages II, p. 12, on US – Underwear, p. 16; on Argentina – Footwear (EC), paras. 81 and 95; on Korea – Dairy; para. 81; on US – Section 211 Appropriations Act, para. 338; and on US – Offset Act (Byrd Amendment), para. 271.

451 The Appellate Body in EC – Computer Equipment stated in para. 109: "Tariff negotiations are a process of reciprocal demands and concessions, of 'give and take'. It is only normal that importing Members define their offers (and their ensuing obligations) in terms which suit their needs. On the other hand, exporting Members have to ensure that their corresponding rights are described in such a manner in the Schedules of importing Members that their export interests, as agreed in the negotiations, are guaranteed. There was a special arrangement made for this in the Uruguay Round. For this purpose, a process of verification of tariff schedules took place from 15 February through 25 March 1994, which allowed Uruguay Round participants to check and control, through consultations with their negotiating partners, the scope and definition of tariff concessions."


should be interpreted as a whole, and, in particular, its sections and parts should be read as a whole.”

7.153 In Canada – Dairy, the Appellate Body made it clear again that a treaty interpreter cannot lightly assume that a WTO Member projected no demonstrable purpose on a specific provision of its schedule:

"In interpreting the language in Canada's Schedule, the Panel focused on the verb 'represents' and opined that, because of the use of this verb, the notation was no more than a 'description' of the 'way the size of the quota was determined'. The net consequence of the Panel's interpretation is a failure to give the notation in Canada's Schedule any legal effect as a 'term and condition'. If the language is merely a 'description' or a 'narration' of how the quantity was arrived at, we do not see what purpose it serves in being inscribed in the Schedule. The Panel, in other words, acted upon the assumption that Canada projected no identifiably necessary or useful qualifying or limiting purpose in inscribing the notation in its Schedule. The Panel thus disregarded the principle of effectiveness in its interpretive effort." (emphasis added)

7.154 The Panel considers, therefore, that in the interpretation of Footnote 1 to Section II, Part IV of the EC's Schedule it must use its best endeavours to give due meaning to the said Footnote and respect the principle of effective treaty interpretation.

(iv) The issue of "conflict" between provisions of a Member's Schedule and provisions of the Agreement on Agriculture

7.155 The Panel recalls that in international law, there is a presumption against conflicts when treaties have the same membership. This principle has been recognized by the WTO jurisprudence when dealing with internal conflicts within the WTO Agreement which includes Members' Schedules. The WTO jurisprudence has maintained the general principle that there is a conflict only when two provisions are mutually exclusive, that is when only one provision "applies" because it is not possible for a single measure to be consistent with both provisions.

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Alcoholic Beverages, supra, footnote 41, p. 12; and Appellate Body Report, India – Patents, supra, footnote 21, para. 45.


457 "... [T]echnically speaking, there is a conflict when two (or more) treaty instruments contain obligations which cannot be complied with simultaneously. ... Not every such divergence constitutes a conflict, however. ... Incompatibility of contents is an essential condition of conflict." (Encyclopedia of Public International Law (North-Holland 1984), p. 468. See also Ian Sinclair, Vienna Convention, 1984, at p. 97.) … a conflict of law-making treaties arises only where simultaneous compliance with the obligations of different instruments is impossible. ... There is no conflict if the obligations of one instrument are stricter than, but not incompatible with, those of another, or if it is possible to comply with the obligations of one instrument by refraining from exercising a privilege or discretion accorded by another. For, in such a case, it is possible for a State which is a signatory of both treaties to comply with both treaties at the same time. (…) The presumption against conflict is especially reinforced in cases where separate agreements are concluded between the same parties, since it can be presumed that they are meant to be consistent with themselves, failing any evidence to the contrary."

458 In the WTO context, see the Panel Report on Indonesia – Automobile at paras.14.29-14.36 and 14.97 to 14.99; the Appellate Body Reports on Guatemala – Cement I at para. 60; on US – Hot Rolled Steel, paras. 55-62. Recently in EC – Tariffs Preferences, para. 88, the Appellate Body seems to have expanded the concept of conflicts to include situations where a provision gives a right while another one gives an obligation.
7.156 The Panel is also aware of the WTO jurisprudence that has established the relationship between provisions of a WTO agreement and provisions of a Member's Schedule. For instance, the Appellate Body in EC – Bananas III concluded, as the GATT panel report on US – Sugar, that:

"The market access concessions for agricultural products that were made in the Uruguay Round of multilateral trade negotiations are set out in Members' Schedules annexed to the Marrakesh Protocol, and are an integral part of the GATT 1994. By the terms of the Marrakesh Protocol, the Schedules are 'Schedules to the GATT 1994', and Article II:7 of the GATT 1994 provides that "Schedules annexed to this Agreement are hereby made an integral part of Part I of this Agreement'. With respect to concessions contained in the Schedules annexed to the GATT 1947, the panel in United States - Restrictions on Importation of Sugar ("United States - Sugar Headnote") found that:

... Article II permits contracting parties to incorporate into their Schedules acts yielding rights under the General Agreement but not acts diminishing obligations under that Agreement."

7.157 The same principle was reiterated in EC – Poultry and in Chile – Price Band System. In the Panel's view, GATT and WTO jurisprudence indicate that WTO Members may use entries in their schedules of concession to clarify and qualify the "concessions" they individually agree to assume in their Schedules but not to reduce or conflict with the obligations they have assumed under the GATT or the WTO Agreement, including the Agreement on Agriculture.

7.158 The Panel notes that the jurisprudence cited above deals with tariff concessions and this includes market access commitments within the meaning of Article 1(g) of the Agreement on Agriculture. The "export subsidy commitments" contain limitations on subsidization, constituting exceptions to the Article 8 general prohibition, and are incorporated into the Agreement on Agriculture through Article 3.1 of the Agreement on Agriculture. The Panel recalls also that contrary to tariff concessions, export subsidy commitments are not renegotiable under Article XXVIII of the GATT 1994. Therefore, export subsidy commitments are different from tariff and other market access concessions. However, in the Panel's view, the principle that scheduled commitments cannot overrule or conflict with the basic obligations contained in a WTO multilateral trade agreement, unless explicitly authorized, remains valid and applicable to export subsidy commitments scheduled in Section II, Part IV of Members' Schedules.

7.159 The Panel believes that this same principle is recognized in Article 8 of the Agreement on Agriculture.

460 GATT Panel Report on US – Sugar, paras. 5.2-5.3.
461 The Appellate Body Report on EC – Poultry, para. 98 stated: "In United States - Restrictions on Imports of Sugar, the panel stated that Article II of the GATT permits contracting parties to incorporate into their Schedules acts yielding rights under the GATT, but not acts diminishing obligations under that Agreement. In our view, this is particularly so with respect to the principle of non-discrimination in Articles I and XIII of the GATT 1994. In EC – Bananas, we confirmed the principle that a Member may yield rights but not diminish its obligations and concluded that it is equally valid for the market access concessions and commitments for agricultural products contained in the Schedules annexed to the GATT 1994. "The ordinary meaning of the term "concessions" suggests that a Member may yield or waive some of its own rights and grant benefits to other Members, but that it cannot unilaterally diminish its own obligations."
462 The Appellate Body Report on Chile – Price Band System, para. 272 stated: "We have observed in a previous case that "[t]he ordinary meaning of the term 'concessions' suggests that a Member may yield rights and grant benefits, but it cannot diminish its obligations". A Member's Schedule imposes obligations on the Member who has made the concessions."
7.160 In this respect, the Panel notes that Article 8 of the Agreement on Agriculture covers various types of commitments in the context of the implementation period; commitments limiting subsidization (Article 3.1), and commitments relating to limitations on the extension of the scope of export subsidization (Article 9.3).

7.161 At the same time, Article 8 makes clear that a Member must at all times comply with the Agreement on Agriculture (and its Schedule). Therefore, a Members' Schedule cannot provide for non-compliance with provisions of the Agreement on Agriculture. Provisions in Members' Schedules relating to commitments authorized by the Agreement on Agriculture may therefore only qualify such commitments to the extent that the said qualification does not act so as to contradict or conflict with the Members' obligations under the Agreement on Agriculture.

7.162 In US – FSC, the Appellate Body recognized the difference between the rule-based provisions contained in the Agreement on Agriculture and the more narrow reduction commitments contained in Members' Schedules.

"The word 'commitments' generally connotes 'engagements' or 'obligations'. Thus, the term 'export subsidy commitments' refers to commitments or obligations relating to export subsidies assumed by Members under provisions of the Agreement on Agriculture, in particular, under Articles 3, 8 and 9 of that Agreement. (...)"

We also find support for this interpretation of the term "export subsidy commitments" in Article 10 itself, which draws a distinction, in sub-paragraphs 1 and 3, between 'export subsidy commitments' and 'reduction commitment levels'. In our view, the terms 'export subsidy commitments' and 'reduction commitments' have different meanings. 'Reduction commitments' is a narrower term than 'export subsidy commitments' and refers only to commitments made, under the first clause of Article 3.3, with respect to scheduled agricultural products. It is only with respect to scheduled products that Members have undertaken, under Article 9.2(b)(iv) of the Agreement on Agriculture, to reduce the level of export subsidies, as listed in Article 9.1, during the implementation period of the Agreement on Agriculture. The term 'export subsidy commitments' has a wider reach that covers commitments and obligations relating to both scheduled and unscheduled agricultural products. (underlining added)

7.163 The Panel is of the view that the "wider" export subsidy obligations provided for in the Agreement on Agriculture cannot be deviated from in a Member's Schedule containing narrower commitments. Members may include in their Schedules reduction commitments as well as other specific types of commitments which, by their nature, are narrower and thus cannot be used to circumvent the broader rule-based export subsidy commitment of the Agreement on Agriculture.

7.164 As discussed in paragraphs 7.127-7.134 above, commitments with respect to export subsidies are thus strictly regulated under the Agreement on Agriculture. Among other disciplines, Article 3 provides that export subsidies must be expressed both in terms of budgetary outlays and in terms of

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463 The Panel recalls the wording of Article 8 of the Agreement on Agriculture: "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." (emphasis added)


465 (footnote original) The term "reduction commitments" also appears in the chapeau to Article 9.1.

466 (footnote original) Article 9.2(b)(iv) provides that, with respect to scheduled products, the budgetary outlay and quantity commitment levels must, by the end of the implementation period, not exceed certain threshold levels, expressed as a percentage of the 1986-1990 base period levels.

quantities; moreover, to be consistent with the Agreement on Agriculture, all such export subsidies must have been subject to reduction commitments pursuant to Articles 3 and 9.1 (and 9.2(b)(iv)).

7.165 Having these guidelines in mind and recalling the Appellate Body ruling in Korea – Dairy that it is "the duty of any treaty interpreter to 'read all applicable provisions of a treaty in a way that gives meaning to all of them, harmoniously'" the Panel needs to see whether the content of Footnote 1 of the EC's Schedule on the one hand, and the European Communities' obligations pursuant to Articles 3, 8 and 9 of the Agreement on Agriculture on the other hand, can be read "harmoniously" or whether the content of Footnote 1 – being inconsistent and conflicting with the European Communities' basic obligations under the Agreement on Agriculture – should be considered without any legal effect and would thus not enlarge or otherwise modify the commitment level specified in Section II, Part IV of the European Communities' Schedule.

7.166 The Panel proceeds first to the interpretation of Footnote 1 to assess whether, as suggested by the European Communities, it provides for a WTO-consistent limitation of 1.6 million tonnes for export subsidies corresponding or equivalent to the amount of imports of ACP/Indian origin.

(v) Interpretation of the European Communities' Footnote 1 on ACP/India sugar:

7.167 Footnote 1 to the entry for sugar in the European Communities' export subsidy commitments reads as follows:

"Does not include exports of sugar of ACP and Indian origin on which the Community is not making any reduction commitments. The average of export in the period 1986 to 1990 amounted to 1.6 mio t."

7.168 The Panel refers to the European Communities' interpretation of Footnote 1:

"Both sentences of the footnote are relevant in order to fully understand the EC's commitments. The footnote is numbered (1) and is found next to the term 'sugar' in the column entitled "description of products", thus applying to the full entry. The first sentence has two elements to it. First, it confirms that exports of an equivalent amount of ACP/Indian sugar were not included in the quantities and outlays reported by the EC for the base period level (1986-1990) which served as a basis for the figures set out in the table. Since the footnote applies to the entire entry, it applies to both the base outlays and base quantities. That is, it indicates the basis for the base quantity and outlay levels. The EC made this clear in the supporting tables which all participants in the negotiations were required to submit. Indeed, Australia explicitly accepts that ACP equivalent sugar was excluded from the supporting tables. The second element of the first sentence makes it clear that exports of the quantity of ACP/India sugar imported shall not be counted against the commitments made on the base period levels (this is the logical concomitant of the non-inclusion of these exports in the base period).

\footnote{Appellate Body Report on Korea – Dairy, para. 81.}

\footnote{Appellate Body Report, United States – Gasoline, supra, footnote 12, p. 23; Appellate Body Report, Japan – Alcoholic Beverages, supra, footnote 41, p. 12; and Appellate Body Report, India – Patents, supra, footnote 21, para. 45.}

\footnote{Exhibit EC– 5.}

\footnote{Australia's first written submission, Annex 1, paras. 4 and 5.}
It is the second sentence which is vital to understanding the footnote (and which is entirely ignored by the Complainants). It expresses the "average of export" of ACP/India equivalent sugar in the period 1986-1990. This sentence cannot be disregarded. It is deprived of meaning if it is considered as merely a statement of fact or a narration of particular circumstances. The reference to the period 1986-1990 (which was the base period for the reduction commitments) is telling. If, as the Complainants would have it, the footnote is simply an exclusion, there would be no need to insert the second sentence, and no reason to refer to the 1986-1990 base period. The reference to the base period indicates that the EC was committing itself, as it had done for the other component of its exports of sugar, to limit its exports to a level established on the basis of the exports made in the base period. It operates in precisely the same way as the other component of the EC's commitments -- it is a limited authorisation to provide export subsidies.

Therefore, according to a proper interpretation of the footnote the EC has articulated its subsidy commitments in two components. One component sets limits which are subject to reduction, and the second component (the footnote) sets a fixed ceiling. Overall, the EC has reduced its export subsidies on sugar.  

Footnote 1 does not contain any "limitation" on export subsidies of ACP/India sugar

7.169 The Panel does not agree with the European Communities' interpretation of Footnote 1. Firstly, the ordinary meaning of the terms of the Footnote does not indicate any "limitation on export subsidies for sugar" to 1.6 million tonnes. The Panel therefore fails to see any commitment "limiting subsidization".

7.170 The Complainants highlight a number of inconsistencies between: (a) the European Communities' assertion before this Panel that Footnote 1 in the European Communities' Schedule has legal effect and constitutes a "commitment", and that, overall, the European Communities has subjected all export subsidies on sugar to reduction commitments; and (b) the European Communities' own notification practice to omit the data relating to export subsidies of ACP/India "equivalent" sugar, as well as its responses to requests for clarification, in the Committee on Agriculture. The Complainants submit that, if the European Communities had been of the view that it had assumed export subsidy reduction commitments in respect of sugar of ACP and Indian origin, it would have provided statistics on the export of such sugar in its notifications, or explained why it did not notify the exports of sugar that it claimed to be covered by its reduction commitments.

7.171 The European Communities does not reconcile the inconsistencies highlighted by the Complainants. Instead, the European Communities sustains that it has consistently interpreted the Footnote in the same manner since 1995, based on the application of the Vienna Convention rules of interpretation. The European Communities insists that it has undertaken to limit subsidization in respect of ACP/India equivalent sugar and that it has reduced its overall commitment on export subsidies on an annual basis.

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472 (footnote original) See, for instance, the Appellate Body Report in Canada – Dairy at para. 135. In that case, the Appellate Body admonished the panel for failing to give meaning to a condition in Canada's goods schedule which the panel had considered was no more than a "description".

473 European Communities' first written submission, paras. 167-169.

474 European Communities' oral statement at the first substantive meeting of the Panel, para. 31.
7.172 The European Communities suggests that the evidence\textsuperscript{475} demonstrates that it has considered and treated 1.6 million tonnes as a "cap" on the amount of exports which can benefit from export subsidies as ACP/India equivalent sugar. For the European Communities, the sugar CMO is managed in order to respect this limit, which forms an integral part of the regulatory structure of the regime. Indeed, since the export refunds are maintained at the difference between the world and the Community price (and thus the Community authorities have limited control over the evolution of the amount of individual refunds) the limits imposed by the WTO Agreements are respected through the control of the quantity of products which may be exported with the benefit of a refund (see Article 27(14) of Regulation 1260/2001).\textsuperscript{476} The Commission verifies on a weekly basis that the export refunds granted stay within the limits set out in the WTO Agreement which permits the Commission to ensure that export refunds are not granted which might exceed the EC’s export subsidy commitments.

7.173 The Panel recalls the Appellate Body's reliance, in Korea – Various Measures on Beef, on statements and notifications by Members before the Committee on Agriculture\textsuperscript{477}, as evidence of a Member's consistent treatment of its commitments under the Agreement on Agriculture.

7.174 The Panel first observes that the EC notifications to the Committee on Agriculture do not suggest that Footnote 1 constitutes a limitation on subsidization.\textsuperscript{478} The European Communities, rather, appears to argue that Footnote 1 exempts it from any export subsidy reduction commitment with respect to sugar of ACP and Indian origin. Indeed, since the entry into force of the WTO Agreement, the European Communities has consistently indicated, in Footnote 5 to its Table ES:1 notifications to the Committee on Agriculture, that the information presented:\textsuperscript{479}

"Does not include exports of sugar of ACP and Indian origin on which the Community has no reduction commitments."

7.175 The Panel also notes that, during the review process (25-26 June 1998 and 17-18 November 1998) undertaken by the Committee on Agriculture pursuant to Article 18 of the Agreement on Agriculture, the European Communities stated, \textit{inter alia}, that:

"Exports of ACP and Indian sugar are eligible to receive export refunds. As mentioned in the EC's Schedule, no reduction commitment is made on this category of sugar."\textsuperscript{480}

and

"As indicated in footnote 1 of the table on export subsidies contained in Part IV, Section II of Schedule CXL, the EC is not undertaking any reduction commitment on exports of ACP or Indian sugar. Consequently, any financial assistance is not

\textsuperscript{475} See European Communities' first submission, table 10. The Panel notes that Australia raised the issue of the statistical inaccuracy of the tables cited by the European Communities, Australia's oral statement at the first substantive meeting, para. 54 and Australia's oral statement at the second Panel meeting, para. 51.

\textsuperscript{476} European Communities' first submission, paras. 175-184.

\textsuperscript{477} Appellate Body Report on Korea – Various Measures on Beef, paras. 103-105.

\textsuperscript{478} The Panel recalls that the practice of a Member may be relevant in the interpretation of that Members' schedule. See the Appellate Body report on EC – Computer Equipment, para. 92.

\textsuperscript{479} Exhibit COMP-17, Footnote (5) to Table ES:1 notifications.

\textsuperscript{480} See G/AG/R/17, p. 59. See also G/AG/R/11.
reported to the WTO. For information, these exports amount to approximately 1.6 million tonnes per year.481

7.176 The Panel must assume that the European Communities has been complying with the notification requirements adopted by the Committee on Agriculture482, and is thus puzzled by the fact that the European Communities has not reported the amounts of actual subsidized quantities and budgetary outlays corresponding to exports of sugar of ACP and Indian origin. In the Panel's view, therefore, the European Communities' notification practice since the entry into force of the WTO Agreement suggests that the European Communities has not assumed a commitment to limit subsidization of sugar of ACP or Indian origin. Importantly, this implies that the European Communities itself has not "treated" the Footnote as a commitment specified in its Schedule. This is inconsistent with the European Communities' claim that it has indeed assumed ceiling level commitments, with respect to the volume of subsidized exports of sugar of ACP and Indian origin.483

7.177 Background documents compiled by the Secretariat on the basis of Members' Schedules and notifications commented on by Members lend support to the Panel's analysis.484 No commitment, whether in the form of budgetary outlays, or quantity, reduction commitment, has ever been recorded, or reflected in any way, in relation to sugar of ACP and Indian origin. The European Communities has not availed itself of the opportunity to update the information contained in such documents in order to clarify that its export subsidy commitments for sugar were articulated in two distinct components. Since the fixed ceiling and the fixed quantity commitments have never been accounted for in the summary tables in respect of EC sugar, the implications are, in the Panel's opinion, that the "understanding" of WTO Members, of the Committee on Agriculture, was that the Footnote was not a commitment assumed by the European Communities. Moreover, the Panel understands that the European Communities has not reacted, nor objected, to the data presented in the Secretariat papers.

7.178 The Panel, therefore, does not find any evidence that the European Communities itself was of the view, during the entire implementation period, that ACP/Indian sugar was another "component" of its commitments. Cumulated with the inconsistency of the European Communities' statements before the Committee on Agriculture and this Panel485; the inconsistency between the information contained in its notifications and its assertions before the Panel486; the Panel concludes that the Footnote has never been "treated" or considered by the members of the Committee on Agriculture, nor by the European Communities, as a "commitment" "specified" in the European Communities' Schedule.487

7.179 The Panel is of the view that the ordinary meaning of the terms indicates that the European Communities is not making a commitment limiting subsidization on exports of sugar of ACP/India origin. On the contrary, the terms of Footnote 1 indicate that the European Communities is making a

481 See G/AG/R/17, p. 29: This reply was provided in response to the US query regarding the application of internal EC prices less transportation costs to imported sugar, and a query regarding the prices applying to imported sugar, which is refined in Europe. The United States sought information as to whether this financial assistance was reported to the WTO, and as to the magnitude of such financial assistance. After hearing the EC reply, the United States stated that it assumed that "no reduction commitment" did not mean that the EC had no commitment at all as regards export subsidization of agricultural products. To the extent that WTO rules exist on the subject, the United States hoped to see more information on sugar exports under the EC financial support programme in future.

482 See G/AG/2.

483 European Communities', first written submission, paras. 174-186.


485 Underlined by the Complainants in para. 4.198 above.

486 See para. 4.199 above.

487 Despite the European Communities' assertions to the contrary referred to in paras. 4.204 to 4.207 above.
statement that exports of subsidized sugar of ACP/Indian origin will not be subject to the reduction commitments provided for in Articles 3, 9.1 and 9.2(b)(iv) of the Agreement on Agriculture.

Footnote 1 does not provide for any commitment for sugar "equivalent" from ACP/India

7.180 The Panel is also of the view that the ordinary meaning of the terms of Footnote 1 does not provide that an amount of subsidized sugar "equivalent" to the amount of sugar imported from ACP/India will be maintained for export. In the Panel's view, the Footnote appears to require that the sugar exports excluded from export reduction commitments actually be sugar of ACP and Indian origin, as stated in Footnote 1. Payment of export subsidies on an equivalent amount of sugar sourced from the European Communities does not come within the terms of the Footnote. For the European Communities, the second sentence makes it clear that it was dealing with exports and therefore, since it does not export or re-export ACP/India sugar as such, it could only be exports equivalent to what it imports from ACP/India. The European Communities adds that Members were aware at the time of the Uruguay Round that it was exporting a quantity of sugar equivalent to what it imports from those countries. The Panel notes, however, that the European Communities today considers that it needs to use wording different from what it used when it scheduled its footnote, and a wording different from what it used in its cover letter when the EC Ambassador transmitted the said EC's Schedule – which seems to indicate that the European Communities did not choose the most appropriate/clear wording at the time.

7.181 The European Communities and some of the third parties referred to the linkages between the Cotonou Agreement and the Sugar Protocol on the one hand and the EC sugar
regime (including the ACP/India equivalent sugar) on the other hand; they added that Members were aware since the 1970s that the Footnote related to a quantity of exports equivalent to the quantity of sugar it imports from ACP countries and India and that this portion of its subsidized exports should be entitled to differential treatment which is, according to the European Communities, articulated in the ACP/India Footnote.

7.182 The Panel agrees with the Complainants that, pursuant to the Sugar Protocol and the EC/India Agreement, the quantity of sugar to be provided by the ACP and India is not contingent on export by the European Communities of that sugar or its equivalent. Moreover, the amount of sugar covered by the Sugar Protocol is 1,294,700 tonnes while the Footnote refers to 1.6 million tonnes. In addition, the Sugar Protocol as included in the Cotonou Agreement, obliges the European Communities to buy certain quantities of sugar from selected ACP countries and India, but does not oblige the European Communities to subsidize re-exports of ACP/India equivalent sugar. Finally, in the Sugar Protocol, the pricing arrangement for purchase of sugar from ACP countries and India is not linked in any way to exports of "ACP/India equivalent" sugar, nor, indeed, to the provision of export subsidies by the European Communities. The Panel is of the view that the Sugar Protocol, even if considered "context" within the meaning of Article 31.2 of the Vienna Convention for the interpretation of Footnote 1, does not support the European Communities' argument.

Conclusion

7.183 In sum, the Panel considers that the ordinary meaning of the terms of Footnote 1 does not indicate any commitment or concessions constituting a limitation on export subsidization or any other type of commitment authorized by the Agreement on Agriculture which could in any way enlarge or otherwise modify the European Communities' commitment level specified in Section II, Part IV of its Schedule. Rather, Footnote 1 constitutes a unilateral statement by the European Communities that, with regard to exports of ACP/India sugar, it is not making any reduction commitment. Moreover, Footnote 1, if it were to constitute such a limitation on subsidization, would only benefit sugar of ACP/Indian origin per se, contrary to the European Communities' suggestion that 1.6 million tonnes of sugar refer to an amount "equivalent" to the amount imported from ACP countries and India.

7.184 Therefore, the Panel concludes that the ordinary meaning of the terms of Footnote 1 does not authorize an additional 1.6 million tonnes of subsidized sugar to be exported corresponding or equivalent to the amount of imports from ACP and India. The content of Footnote 1 therefore does not enlarge or otherwise modify the European Communities' quantity commitment level specified in Section II, Part IV of its Schedule to be 1,273,500 tonnes of sugar per year, or its budgetary outlay commitment of €499.1 million per year, with effect since marketing year 2000/2001.

Can the ACP/India Footnote be regarded as a second component of the European Communities' commitment level that would not be subject to reduction per se but that would form part of the overall European Communities' commitment level which has been reduced?

7.185 Assuming arguendo that the Footnote could be interpreted as providing for a "limitation on subsidization in the form of a ceiling" for a maximum of 1.6 million tonnes, the Panel proceeds now to determine whether the said Footnote, as interpreted by the European Communities, could be WTO consistent and part of the European Communities' overall commitment level with respect to export subsidies on sugar.

annexed to the Lomé Conventions. The sugar protocol has been maintained as such, without modification, throughout the four Lomé Conventions and Cotonou Agreement.

7.186 The Panel has reached the conclusion that all export subsidies scheduled pursuant to Articles 3 and 8 of the Agreement on Agriculture must have been subject to reduction commitments. The European Communities argues that although the ACP/India sugar Footnote acts as a ceiling on subsidization and is not subject to any reduction commitment, the European Communities' overall commitment on export subsidies to sugar has been reduced. According to the European Communities, export subsidies provided for in its Schedule are not inconsistent and in conflict with Article 9.1 and 9.2(b)(iv) of the Agreement on Agriculture, being of the opinion that Article 9.2(b)(iv) is outside the Panel's terms of reference.

7.187 The Panel disagrees with the European Communities. The Panel recalls that the possibility of maintaining export subsidies is an exception to the general prohibition against export subsidies contained in Article 8 of the Agreement on Agriculture. As discussed in paragraphs 7.133-7.135, WTO-consistent export subsidies that could be maintained if and when scheduled, had to be subject to reduction commitments. In other words, export subsidies that were not subject to any reduction commitment could not be maintained, and are prohibited pursuant to Article 8 as interpreted in light of Articles 3 and 9 of the Agreement on Agriculture.

7.188 Moreover, Article 9.1 defines and lists export subsidies which must be subject to reduction. Article 9.1(a) reads as follows:

"The following export subsidies are subject to reduction commitments under this Agreement:

(a) the provision by governments or their agencies of direct subsidies, including payments-in-kind, to a firm, to an industry, to producers of an agricultural product, to a cooperative or other association of such producers, or to a marketing board, contingent on export performance."

7.189 In this context, Article 9.1(a) seems to cover the type of export subsidy provided for in the ACP/India sugar Footnote. Indeed, the European Communities does not deny that its exports of ACP/India equivalent sugar benefit from export subsidies; its argument is essentially that the European Communities is entitled to provide such export subsidies. In the Panel's view, if the European Communities claims that it is entitled to maintain such export subsidies, the said export subsidies must have been subject to reduction commitments.

7.190 The Panel considers that Footnote 1 to Section II of Part IV of the EC's Schedule attempts to reduce and modify the European Communities' obligation pursuant to Articles 3, 8, 9.1 and 9.2(b)(iv) of the Agreement on Agriculture. In the Panel's view, the content of Footnote 1 is fundamentally inconsistent with the basic provisions of the Agreement on Agriculture, as Footnote 1, on the one hand, and Articles 3, 8 and 9 of the Agreement on Agriculture, on the other hand, are mutually inconsistent. Therefore, the content of Footnote 1 contradicts and conflicts with the European Communities' basic obligations contained in Articles 9.1, 9.2(b)(iv), 3 and 8 of the Agreement on Agriculture. Consequently, it is not possible to interpret harmoniously Footnote 1 and the European Communities' basic obligations relating to export subsidies contained in the Agreement on Agriculture.

7.191 The Panel finds, therefore, that the content of Footnote 1 is of no legal effect and does not enlarge or otherwise modify the European Communities' quantity commitment level specified in
Section II, Part IV of its Schedule to be 1,273,500 tonnes of sugar per year, or its budgetary outlay commitment of €499.1 million per year, with effect since 2000/2001.495

The ACP/India Footnote does not contain any budgetary outlays so it cannot consist of an export subsidy consistent with the Agreement on Agriculture.

7.192 The Panel is also of the view that since the ACP/India sugar Footnote does not contain any reference to budgetary outlays, it cannot be considered as a component of a scheduled export subsidy commitment. The European Communities is of the view that Article 3.3 does not require that all export subsidy commitments contain both quantity and budgetary outlays reduction commitments. As mentioned before, the Panel disagrees with the European Communities in this regard. In paragraphs 7.137-7.142 the Panel has reached the conclusion that all export subsidy commitments are to be expressed both in terms of volume and in terms of budgetary outlays, but the European Communities' Footnote does not contain any such budgetary outlay commitment.

7.193 The European Communities adds that Footnote 1 contains a "de facto" budgetary limit of 1.6 million multiplied by the average export refund which can be granted within the first component of the EC's commitments" because the refunds for both types of sugar must be the same. In the Panel's view, what the European Communities describes as a "budgetary limit" does not arise from a commitment it has assumed in its Schedule but from its own practice of according the same subsidies to A and B sugar and to ACP/India equivalent sugar. The European Communities therefore describes it as a "de facto" limit.496

7.194 The Panel considers that there is nothing in the ordinary terms of the Footnote which expresses a legally binding commitment that the per unit subsidization of exports of ACP/India equivalent sugar shall not exceed that for exports of A and B sugar. Moreover, on this construction, the budgetary outlay commitment level cannot be predicted beforehand. It can only be known in retrospect once the European Communities has finished granting export refunds for a particular year. The Panel notes that the purpose of the requirement that reduction commitments be expressed both in terms of quantity and budgetary outlays is to ensure transparency so that Members know in advance what level of export subsidies will be provided on a yearly basis. Limitations resulting from a Member's own domestic law or practices and unknown future events are therefore not compatible with the Agreement on Agriculture.

7.195 The Panel also notes that the European Communities' Council Regulation No. 1260/2001 at issue in this case, explicitly recognizes that "the Agriculture Agreement provides for export support to be reduced, in terms of both the quantities covered and the level of the subsidies involved."497

7.196 Therefore, the Panel concludes that the ACP/India sugar Footnote cannot be reconciled with the requirements of Article 3.3 that reduction commitments be expressed both in terms of quantity and of budgetary outlays. The content of Footnote 1 is thus inconsistent and conflicts with the requirements of Articles 3 and 8 of the Agreement on Agriculture. Accordingly, the content of Footnote 1 is of no legal effect and does not enlarge or otherwise modify the European Communities' quantity commitment level specified in Section II, Part IV of its Schedule to be 1,273,500 tonnes of

495 The Panel agrees with the European Communities that Article 9.2(b)(iv) was not raised as a claim but as an argument (see para. 4.19 above) but this does not preclude the Panel from referring to Article 9.2(b)(iv) as context to Article 3.3 and with a view to understanding the scope of the European Communities' commitment.

496 See also para. 4.192 above.

497 European Communities' Regulation No. 1260/2001, Preamble, recital (10) (emphasis added).
sugar per year, or its budgetary outlay commitment of €499.1 million per year, with effect since 2000/2001. 498

(vi) Conclusion on the legal value and effect of the ACP/India sugar Footnote

7.197 The Panel is therefore of the view that, even if it were to be considered as including a commitment limiting subsidization to 1.6 million tonnes of ACP/India equivalent sugar, which it does not, the content of Footnote 1 to Section II, Part IV of the EC's Schedule is inconsistent and conflicts with Articles 3, 8, 9.1 and 9.2(b)(iv) of the Agreement on Agriculture and as such cannot be read harmoniously with the provisions of the Agreement on Agriculture: it does not provide for any budgetary outlays, and subsidies provided to ACP/India equivalent sugar have not been subject to any reduction. Footnote 1 cannot therefore constitute a second component of the European Communities' overall commitment level for export subsidies on sugar.

7.198 Consequently, the Panel finds that the content of Footnote 1 is of no legal effect and does not enlarge or otherwise modify the European Communities' quantity commitment level specified in Section II, Part IV of its Schedule to be 1,273,500 tonnes of sugar per year, or its budgetary outlay commitment of €499.1 million per year, with effect since 2000/2001.

3. Was the European Communities authorized to deviate from the Agreement on Agriculture's basic obligations through a negotiated departure from the Modalities Paper?

(a) Arguments of the parties 499

7.199 For the European Communities, Footnote 1 is a negotiated departure from the Modalities Paper. The European Communities insists that export subsidy commitments, like tariff concessions, were the subject of detailed (and often very difficult) negotiation during the Uruguay Round. The European Communities' commitments, while applicable to its exports, represent the negotiated balance of the varied interests of all participants in the Uruguay Round. In challenging the Footnote, the Complainants are trying to unsettle that balance. For the European Communities, the claims and objections which the Complainants make in this proceeding were as available to them during the verification process as they are now. Had they been raised during the verification process, and considered valid, the Members concerned could have negotiated a different balance of concessions.

7.200 Moreover, in the context of its claim that the Complainants are acting inconsistently with their good faith obligation pursuant to Article 3.10 of the DSU, the European Communities argues that the Complainants were undeniably aware, by virtue, inter alia, of the very inclusion of the Footnote in the European Communities' export subsidy commitments (both in their draft and final form), of the existence of the European Communities' intended treatment of ACP/India sugar. The European Communities provides correspondence in which the European Communities' Ambassador is allegedly making clear that the European Communities never intended and never undertook any commitment to reduce its export subsidies of equivalent ACP/India sugar and this was known and accepted by the other Members. The European Communities adds also that the Complainants never challenged the European Communities during the verification process. Although the Complainants may have been silent at the time, today they deny concluding any such agreements.

498 The European Communities draws a third analogy between the Footnote and the case of incorporated products, for which only one form of commitment (budgetary) was scheduled, as specifically envisaged in the Modalities Paper. Moreover, the Panel fails to recognize any similarity between the content of Footnote 1 and "incorporated products". The only provision of the Agreement on Agriculture dealing with "incorporated" agricultural products is Article 11, which is of no relevance to the present dispute. 499 See also paras. 4.207 et seq above.
The European Communities also argues that the Modalities Paper authorized Members to deviate from the Modalities Paper.

The Complainants emphasized that the European Communities does not cite any relevant provision of the Modalities Paper that would have permitted it to adopt a lesser obligation than that expressed in the language of paragraphs XI and XII of that text. Nor does the European Communities' assertion found support in Annexes 7 or 8 of the Modalities Paper. Indeed, the Modalities Paper is predicated on basic multilateral commitments. The reduction commitments are multilateral in nature and do not constitute negotiated concessions. Unlike the access commitments, they were 'self-contained' in regard to the balance of concessions.

(b) Assessment by the Panel

The Panel reviewed the evidence presented by the parties in the context of the ACP/India Footnote and notes that at the earlier stages of the negotiations of the EC Schedule, Footnote 1 was not included in the first drafts and that there was no reference to sugar from the ACP countries and India. In the March 1992 EC Draft Schedule, there was no footnote. In the December 1992 EC Draft Schedule, a footnote was included but it was not the present ACP/India Footnote. It read: "the EC reserves the right to maintain flexibility of outlay and budgetary commitments." It would seem that at each stage, contracting parties specifically rejected the European Communities' exclusion of ACP/India sugar from its sugar subsidy base as witnessed by the G8 Technical Discussions on Agriculture Schedules in 1992 and bilateral meetings between the European Communities and other countries (including Australia).

The Panel notes that to support its conclusion that Members "did not object" or that they even "agreed" to the inclusion of the European Communities' Footnote, the European Communities relies on the fact that the cover letter signed by the European Communities' Ambassador transmitting the European Communities' draft schedule underlined the absence of any reduction commitment for ACP/India sugar. For the European Communities, its intentions were made clear. In a letter of 4 March 1992, providing the supporting tables on which the European Communities' export subsidy commitments were based, the European Communities stated:

"On export competition, the Community has not included the volume of sugar corresponding to its imports of sugar from ACP countries. The Community will not take commitments on this part of its sugar exports."

The European Communities presented evidence that in December 1993 Australia was asking whether "ACP [sugar] would still be made without commitments, in relation to export commitments". In doing so, the European Communities seems to imply that Australia was aware that ACP sugar would not be subject to reduction commitments and would therefore have agreed to it.

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500 Exhibit EC-5, EC Letter of 4 March 1992; and European Communities' first written submission, Table 11.
501 Exhibit EC-5, EC Letter of 4 March 1992; and European Communities' first written submission, Table 11.
502 Exhibit EC-4 on Draft schedule of commitments on 16 December 1992.
503 Exhibit ALA-3, ALA-5, ALA-8, Australia’s Oral Statement to the first substantive Panel meeting, paras. 60-66, and Australia’s replies to the Panel’s questions Nos 16 and 17 and EC-7: List of Bilateral Meeting EC/other participants: Australia requests on 17 December 1992 that ACP sugar be included in reduction commitments.
504 Exhibit EC–5, EC Letter of 4 March 1992; and European Communities' first written submission, Table 11.
505 Exhibit EC–8, EC Commission: minutes of the meeting with Australia of 3 December 1993.
However, Australia produced evidence that it had subsequently asked the European Communities to include commitments on all EC export subsidies on sugar.\footnote{Exhibit ALA-5, Australia’s Letter of 10 December 1993 to EC (page 4). The Panel notes that the EC submitted the same document in Exhibit EC-24 but the Panel notes that the page which referred to sugar as an issue for which Australia was requiring settlement was not reproduced. In its Interim Review comments the European Communities informed the Panel that this omission was inadvertent.}

7.206 Soon after, the European Communities reiterated in a letter addressed to the Director General of the GATT and to the Chairman of the TNC that it did not intend to make commitments with regard to ACP/India sugar. On 14 December 1993 the European Communities submitted a revised version of its Schedule and for the first time inserted a footnote in the draft Schedule to this effect.\footnote{Exhibit EC-6, EC Letter of 14 December 1993 to GATT.} The cover letter again contained the statement:\footnote{Exhibit EC-6, EC Letter of 14 December 1993 to GATT.}

"On export competition, the European Communities have not indicated the volume and the budget outlays for sugar corresponding to its imports from ACP countries and India. The European Communities will not take commitments on this part of its exports."

7.207 The same Footnote was included in the final version of the European Communities’ Schedule.\footnote{Exhibit EC–9, Export Subsidy in Schedule LXXX-EC. See also Exhibit EC – 1 and Exhibit COMP-16 on Schedule CXL.} The European Communities considers therefore, that since Footnote 1 was adopted as proposed by the European Communities, without objection from the Complainants, it is legally valid and binding. The European Communities also insists on the fact that a first draft Schedule of commitments on 16 December 1992 and a revised draft on 14 December 1993 were circulated to all participants in the Uruguay Round. The other participants had ample opportunity to react to these two drafts and many did so, including the Complainants. None of them, however, raised any question with respect to Footnote 1 to Section II, Part IV of the EC’s Schedule. The European Communities’ Schedule, like those of the other participants, was submitted on 25 March 1994, following a process of verification which allowed all participants to check and control the commitments.\footnote{See Appellate Body Report on EC–Computer Equipment, paras. 109-110. The Appellate Body emphasized that tariff commitments “represent a common agreement among all Members” and that “any clarification of the scope of tariff concessions that may be required during the negotiations is a task for all interested parties.”} Again, none of the Complainants, or any other participant, formally objected to the said Footnote.

7.208 The Panel examines the evidence produced by Australia and notes that the latter did not seem to accept this "fait accompli".\footnote{Exhibit ALA-8, UR-Aus summary statement 31 January 1994 where Australia outlined that the EC offer of 14 December 1993 has a number of outstanding issues, including that it “does not include subsidies by direct export restitutions (corresponding to its imports of sugar from ACP countries and India) which is inconsistent with the Final Act and open to challenge” (page 2).} Australia noted in a summary statement on 31 January 1994 that the above-mentioned EC offer contained a number of remaining outstanding items, including the fact that the EC sugar commitments in the EC’s Schedule did not include export subsidy reduction commitments for sugar exports subsidized by direct export restitutions (corresponding to imports of ACP/India sugar). The Panel notes that on 23 February 1994 Australia and the European Communities issued a Joint Communiqué from the "Australia-European Commission Ministerial Consultations"\footnote{Australia-European Commission Ministerial Consultations, 23 February 1994, Joint Communiqué.} which reported on the consultations and which, according to the European Communities, illustrated that the European Communities and Australia had "settled outstanding
items”. 513 For Australia, this Press Communiqué does not include all outstanding or settled issues between the parties and, in any case, this Press Communiqué does not have the status of a record of settlement of negotiations.514

7.209 Then, the European Communities wrote to the Deputy Director of the GATT in March 1994 that it would make some changes to its Schedule (though not necessarily all the changes requested by the contracting parties). 515 The European Communities nonetheless continued to include the Footnote in its Schedule and from 1995 onwards notified to the WTO Committee on Agriculture that the data on its subsidized exports “does not include exports of sugar of ACP/Indian origin on which the Community has no reduction commitment.”516

7.210 The Panel also examined evidence produced by the European Communities arguing that Australia was aware that ACP/India sugar had not been included in the reduction commitments made by the European Communities. 517 The Panel considers that the fact that Australia knew and made public its knowledge that ACP/India sugar had not been made part of the reduction commitments does not mean that Australia agreed with the situation. The evidence and submissions produced by all parties show that the Complainants did not agree to any European Communities’ deviations from the Agreement on Agriculture. On the contrary, Australia presented evidence that it had objected to such exclusion from the very beginning of its bilateral discussions with the European Communities, while the other Complainants assert that they had never agreed to such an insertion and deviation from the Agreement on Agriculture.

7.211 In this respect, the Panel refers to the findings of the panel in EC – Bananas (Article 21.5 – EC) stating that silence or failure to challenge a measure by a Member does not create the presumption that said Member has agreed that the measure at stake is consistent with the WTO Agreement. The Panel held:

"We agree with the European Communities that there is normally no presumption of inconsistency attached to a Member's measures in the WTO dispute settlement system. At the same time, we also are of the view that the failure, as of a given point in time, of one Member to challenge another Member's measures cannot be interpreted to create a presumption that the first Member accepts the measures of the other Member as consistent with the WTO Agreement."518

7.212 In the Panel's view, even assuming that the participants in the Uruguay Round were authorized to negotiate departures from the Modalities Paper which is not clear, such negotiated departure would only be relevant to the extent that it is reflected in the European Communities' Schedule and is WTO consistent.519 The acknowledgment of the existence of Footnote 1 or the absence of agreement to the inclusion of said Footnote does not, for the Panel, equal acquiescence on the part of the interested parties. The Panel recalls that in Canada – Dairy, the Appellate Body considered the negotiations which took place with regard to Canada's and the United States' respective

513 European Communities' second oral statement, para. 94.
514 Australia's second written submission, para. 84.
515 Exhibit ALA-7, EC Letter of 25 March 1994 to GATT.
516 See paras. 7.174-7.178.
519 The Panel recalls inter alia that pursuant to Articles 3.2 and 19.2 of the DSU panels "cannot add to or diminish rights and obligations provided in the covered agreements".
Schedules and highlighted that though Canada's commitment had been made unilaterally, they were the result of lengthy negotiations:

"In considering 'supplementary means of interpretation', we observe that the 'terms and conditions' at issue were incorporated into Canada's Schedule after lengthy negotiations between Canada and the United States, regarding reciprocal market access opportunities for dairy products. Both Canada and the United States agree that those negotiations failed to produce any agreement between them."

7.213 Unlike the situation highlighted by the Appellate Body in Canada – Dairy, the parties to the present dispute did not negotiate the inclusion of the Footnote and did not agree or come to an understanding on the value of such exclusion. There is no evidence of any relevant exchanges between the parties or any other form of negotiation, let alone agreement on this subject matter.

7.214 Moreover, the Panel is also of the view that a departure from the basic obligations of the Agreement on Agriculture, in the form of a footnote in the EC's Schedule, could not be considered a "waiver" agreed to by the Uruguay Round participants.

7.215 Under the WTO, waivers are strictly regulated and subject to the procedures of Article IX:4 of the WTO Agreement, including annual reporting to the General Council. This is obviously not the case with Footnote 1 to the European Communities' Schedule, Section II, Part IV. Already under the GATT, the panel in US - Sugar Waiver stated:

"The Panel took into account in its examination that waivers are granted according to Article XXV:5 only in 'exceptional circumstances', that they waive obligations under the basic rules of the General Agreement and that their terms and conditions consequently have to be interpreted narrowly."

7.216 In the Panel's view, the evidence and explanations submitted by the Complainants sufficiently refute the presumption, if any, that silence or lack of challenge would have amounted to agreement that Footnote 1 was in conformity with the WTO Agreement or constituted an agreed departure from the European Communities' basic obligations of the Agreement on Agriculture.

7.217 The Panel bears in mind, as highlighted by the Appellate Body in EC – Hormones, that the duty to make an objective assessment of the facts under Article 11 of the DSU is, among others, "an obligation to consider the evidence presented to a panel and to make factual findings on the basis of that evidence" and the fact that according to the Appellate Body it is "generally within the discretion of the panel to decide which evidence it chooses to utilize in making findings."

7.218 The Panel has examined all the evidence presented to it and has made use of its discretion. In doing so, the Panel takes into account that the Complainants have maintained their opposition to Footnote 1 since the inclusion of the Footnote in the EC Schedule, as evidenced by correspondence and continuous opposition to the EC sugar regime throughout the years. Furthermore, the Panel considers that Australia and the other Complainants, even if they were aware of the purported exclusion of ACP/India equivalent sugar from the European Communities' reduction commitments and remained silent, could not in any event have agreed to such an exclusion on behalf of the WTO.

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520 In addition, the commitment did not limit access to the quota as such and did not diminish the rights of the United States. See Panel Report on Canada – Dairy, footnote 530 to para. 7.155.
membership as it would have nullified or impaired the rights of WTO Members, other than the Complainants. If the Panel were to sanction such a proposition it would be acting contrary to Articles 3.2 and 19.2 of the DSU which deny panels the authority to "add to or diminish the rights and obligations provided in the covered agreements".

7.219 The Panel notes finally the distinction between the present dispute and the situation prevailing in the EC – Bananas III dispute where the WTO-inconsistent measures challenged were "required" by the Lomé Convention some of which benefited from a WTO waiver. In the present dispute, the EC/ACP Waiver authorizes the European Communities to adopt measures inconsistent with Article I of the GATT 1994 in favour of imports of sugar from ACP countries but the Cotonou Agreement or Sugar Protocol do not require the European Communities to subsidize exports of sugar imported from the ACP countries, even less so if this is inconsistent with the Agreement on Agriculture.

7.220 The Panel concludes therefore that participants in the Uruguay Round and WTO Members did not agree to the European Communities' inclusion of Footnote 1 as an agreed departure to the European Communities' basic obligations under the Agreement on Agriculture.

4. Conclusion on the European Communities' commitment level for exports of subsidized sugar

7.221 The Panel is therefore of the view that, even if it were to be considered to include a commitment limiting subsidization for 1.6 million tonnes of ACP/India equivalent sugar, which it does not, Footnote 1 to Section II, Part IV of the EC's Schedule is inconsistent and conflicts with Articles 3, 8 and 9 of the Agreement on Agriculture and as such cannot be read harmoniously with the provisions of the Agreement on Agriculture. The content of Footnote 1 cannot constitute a second component of the European Communities' overall commitment level for export subsidies on sugar. Moreover, Footnote 1 cannot constitute an agreed departure from the European Communities' basic obligations under the Agreement on Agriculture.

7.222 The Panel finds, therefore, that the content of Footnote 1 is of no legal effect and does not enlarge or otherwise modify the European Communities' quantity commitment level specified in Section II, Part IV of its Schedule to be 1,273,500 tonnes of sugar per year, or its budgetary outlay commitment of €499.1 million per year, with effect since 2000/2001.

E. IS THE EUROPEAN COMMUNITIES EXPORTING SUBSIDIZED SUGAR IN QUANTITIES EXCEEDING ITS LEVEL OF COMMITMENT CONTRARY TO ARTICLES 3, 8 AND 9 OF THE AGREEMENT ON AGRICULTURE?

1. The burden of proof of Article 10.3 of the Agreement on Agriculture

7.223 The Panel recalls that the Complainants have claimed that the European Communities is in breach of Articles 3 and 8, alleging that the European Communities is subsidizing and exporting a scheduled product, in casu sugar, in amounts exceeding its scheduled commitment level.

7.224 In this context, the Complainants have invoked the application of Article 10.3 of the Agreement on Agriculture.

7.225 Article 10.3 of the Agreement on Agriculture provides special rules on burden of proof:

\[\text{\footnotesize \textsuperscript{525}}\text{ Waiver decision WT/MIN(01)/15.}\]

\[\text{\footnotesize \textsuperscript{526}}\text{ See Section IV.C above.}\]
"Any Member which claims that any quantity exported in excess of a reduction commitment level is not subsidized must establish that no export subsidy, whether listed in Article 9 or not, has been granted in respect of the quantity of exports in question."

7.226 With regard to Article 10.3, the Appellate Body in Canada – Dairy (Article 21.5 – New Zealand and US II) has stated that:

"Consistent with the usual rules on burden of proof, it is for the complaining Member to prove the first part of the claim, namely that the responding Member has exported an agricultural product in quantities that exceed the responding Member's quantity commitment level.

(...) The significance of Article 10.3 is that, where a Member exports an agricultural product in quantities that exceed its quantity commitment level, that Member will be treated as if it has granted WTO-inconsistent export subsidies, for the excess quantities, unless the Member presents adequate evidence to "establish" the contrary."

7.227 Article 10.3 is such that once the Complainants have factually proven that the European Communities is exporting sugar in quantities exceeding its commitment levels, there is a shift in the burden of proof and it is then for the European Communities to prove that the sugar it exports in quantities exceeding its commitment level is "not" subsidized. "Article 10.3 thus acts as an incentive to Members to ensure that they are in a position to demonstrate compliance with their quantity commitments under Articles 3.3 and 8 of the Agreement on Agriculture. This reversal of the usual rules on the burden of proof obliges the European Communities to "bear the consequences of any doubts concerning the evidence of export subsidization."

7.228 The Panel notes the European Communities' argument that "the [C]omplainants would impose an impossible task of identifying all the conceivable export subsidies that it does not grant."

7.229 In the Panel's view, this is not the European Communities' task. Instead, the European Communities must provide prima facie evidence that excess exports of sugar are not subsidized. A respondent (as the European Communities is in the present dispute) should be able to, or may be able to, make a demonstration that the measure is not caught by one or other of the definitions in Article 9.1(a) to (f) of the Agreement on Agriculture. The respondent should also be able to demonstrate that the challenged measure is not a "subsidy contingent upon export performance" within the meaning of Article 1(e) of the Agreement on Agriculture. The European Communities should be aware of its obligations under the Agreement on Agriculture and should also be cognisant of its subsidies programmes. This general principle is recognized also in Article XVI:4 of the WTO Agreement which provides that "Each Member shall ensure the conformity of its laws, regulations and administrative procedures with its obligations as provided in the annexed Agreements". The requirements of Article 10.3 of the Agreement on Agriculture are based on the assumption that Members are aware of the subsidies they provide to their own producers. If there are, in fact, no subsidies, the European Communities should be able to make this demonstration.

527 Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US II), paras. 72 and 74; see also paras. 67 to 75 of the same Appellate Body Report.


529 European Communities' reply to the Panel question No. 4.
2. The application of the special rule on the burden of proof to this dispute

(a) The quantitative aspect

The Complainants have provided prima facie evidence that from 1995, the European Communities has been exporting sugar in quantities exceeding its commitment level. In particular, while the European Communities' export subsidies commitment level was for 1,273,500 tonnes of sugar for the 2000/2001 marketing year, its actual sugar exports amounted to 4,097,000 tonnes, that is some 2,823,500 tonnes in excess of its commitment level.

(b) The subsidization aspects of the claim

Having reached the conclusion that the European Communities has exceeded its commitment level for exports of subsidized sugar every year since 1995 and in particular in the marketing year 2000/2001, the Panel now proceeds to examine the European Communities' argumentation that its excess exports of sugar are not subsidized. The Panel agrees with the Complainants that the essential fact is that the total quantity of sugar exported by the European Communities exceeds its commitment level for sugar. The Panel understands that sugar in excess of the European Communities' commitment level is essentially composed of ACP/India equivalent sugar and C sugar. The Complainants argue that ACP/India equivalent sugar, and C sugar, are respectively subsidized within the meaning of Article 9.1(a) and (c) of the Agreement on Agriculture. The Panel therefore proceeds to examine the Complainants' arguments in turn.

3. Has the European Communities demonstrated that its exports of ACP/India equivalent sugar are not subsidized?

(a) Arguments of the parties

The Complainants claim that in each of the last five years, the European Communities' total export of sugar exceeds its commitment levels. For instance, the Complainants argue that during the marketing year 2001-2002, the European Communities had exported 1,725,100 tonnes of ACP/India equivalent sugar alone: such subsidized exports were in excess of the European Communities' scheduled commitment level of 1,273,500 tonnes.

The Complainants recalled that, if the European Communities claimed that the exports of ACP/India "equivalent" sugar were not subsidized, it had the burden of proof, under Article 10.3 of the Agreement on Agriculture, to establish that no export subsidies applied to such exports. The Complainants submitted that the European Communities granted export subsidies listed in Article 9.1(a) of the Agreement on Agriculture to exports of ACP/India equivalent sugar. The export refunds granted to ACP/India equivalent sugar were the same per unit as the export refunds granted to A and B quota sugar and thus these payments clearly constituted "direct subsidies" provided by government, to firms, to the exporting industry and to producers of sugar, (an agricultural product), and were "contingent on export performance", within the meaning of Article 9.1(a) of the Agreement.

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530 See also the parties' arguments with respect to the burden of proof in paras. 4.25-4.35 above.
531 EC sugar commitment levels as stated in Section II of Part IV of the European Communities' Schedule CXL of the EC-15. Actual export quantities taken from "Notification concerning export subsidy commitments (Tables ES:1 to ES:3). It is noted that the EC notifications of its commitment levels were expressed as "white sugar equivalent" and its notified total exports are expressed in "product weight basis". Any resulting differentiations in variables will not have an effect on the Panel's analysis of the EC's commitments and exportation beyond its commitment levels because the amount of actual exports will still be well above commitment levels regardless of any change as a result of any calibration between "white sugar equivalent" and "product weight basis" figures. See also Annex C.
532 See also paras. 4.175-4.180 above.
on Agriculture. Consequently, the European Communities acted inconsistently with its obligations under Articles 3.3 and 8 of the Agreement on Agriculture.

7.234 The European Communities does not deny that ACP/India equivalent sugar benefits from the same level of export refunds per unit as A and B sugar do. It claims essentially that the amount of ACP/India equivalent sugar that it exports is included in its commitment level pursuant to Article 3.3 of the Agreement on Agriculture.

(b) Assessment by the Panel

7.235 The Panel recalls that the European Communities does not deny the Complainants' allegation that ACP/India equivalent sugar benefits from the same level per unit of export refunds as A and B sugar do; the European Communities does not refute either the Complainants' claim that exports of ACP/India equivalent sugar are subsidized within the meaning of Article 9.1(a) of the Agreement on Agriculture which reads as follows:

"The following export subsidies are subject to reduction commitments under this Agreement:

(a) the provision by governments or their agencies of direct subsidies, including payments-in-kind, to a firm, to an industry, to producers of an agricultural product, to a cooperative or other association of such producers, or to a marketing board, contingent on export performance."

7.236 The Panel recalls that "a prima facie case is one which, in the absence of effective refutation by the defending party, requires a panel, as a matter of law, to rule in favour of the complaining party presenting the prima facie case". 533

7.237 Pursuant to Article 10.3 of the Agreement on Agriculture, the Panel reaches the conclusion that the European Communities has not demonstrated that its exports of ACP/India equivalent sugar are not subsidized, as the evidence indicates that exports of what the European Communities considers to be ACP/India equivalent sugar receive export subsidies within the meaning of Article 9.1(a) of the Agreement on Agriculture.

7.238 The Panel concludes that since 1995, the European Communities has been exporting what it considers to be ACP/India equivalent sugar with export subsidies in quantities exceeding its commitment level of 1,273,500 tonnes. In doing so the European Communities has been acting inconsistently with Articles 3 and 8 of the Agreement on Agriculture.

4. Has the European Communities demonstrated that its exports of C sugar are not subsidized?

(a) Introduction

7.239 The Panel recalls that since 1995 the European Communities' total exports of sugar far exceed its commitment levels. In particular, since the marketing year 2000/2001, the European Communities' commitment level is for 1,273,500 tonnes of sugar while its total exports of sugar for that same year were 4,097,000 tonnes (some of which were ACP/India equivalent sugar already found to be inconsistent with Articles 3 and 8 of the Agreement on Agriculture.)

7.240 In Canada – Dairy (Article 21.5 – New Zealand and US II), the Appellate Body interpreted Article 10.3 of the Agreement on Agriculture to mean that “where a Member exports an agricultural product in quantities that exceed its quantity commitment level, that Member will be treated as if it has granted WTO-inconsistent export subsidies, for the excess quantities, unless the Member presents adequate evidence to ‘establish’ the contrary.”\(^{534}\) The Panel has already reached the conclusion that the European Communities’ exports of its ACP/India equivalent sugar are inconsistent with its obligations under Articles 3 and 8 of the Agreement on Agriculture.\(^{535}\) The Panel examines hereafter whether the European Communities has proven satisfactorily that its exports of C sugar are not and were not subsidized in any manner.

(b) Arguments of the parties\(^{536}\)

7.241 The Complainants argue that the European Communities has created a legal framework that: (i) encourages the overproduction of sugar; (ii) segregates the export market for C sugar completely from the domestic market by imposing sanctions for failure to export such sugar; and (iii) generates the profits and capital used to fund the below production cost exports of that sugar. This legal framework contemplates various payments within the meaning of Article 9.1(c) of the Agreement on Agriculture in relation to C sugar production and exports. The Complainants mainly contend that EC sugar producers receive a payment as evidenced by the fact that C sugar is being exported at prices that do not reflect its proper value because the price received does not cover its average total cost of production. Accordingly, C sugar is receiving a payment. The Complainants also refer to payments by way of below cost of production sales of C beet to C sugar producers. Under the above analysis, the Complainants argue that C beet, an input in C sugar, priced at below cost of production, serves as a payment resulting in an export subsidy as defined by Article 9.1(c) of the Agreement on Agriculture.

7.242 The European Communities responds essentially that C sugar does not involve any payment within the meaning of Article 9.1(c) of the Agreement on Agriculture. It argues that export sales of C sugar into the world market is the only form of alleged payment that is brought by the Complainants before the Panel within the Panel’s terms of reference and finds that cost of production is not a relevant benchmark for such a payment in this dispute. The European Communities argues further that world market prices should be the relevant benchmark in this dispute and, accordingly, does not find any payments. In addition to arguing that the other forms of alleged payment that the Complainants have put forward are outside the Panel’s term of reference, the European Communities claims that the alleged payments do not offer any benefits to EC sugar producers.\(^{537}\)

7.243 The Complainants argue that there is a demonstrable link between the payments and the governmental action in the present dispute. They argue that the payments that allow C sugar to be produced below its cost of production arise from governmental action regulating the entire EC sugar industry. They claim that EC sugar producers can make the below cost of production sales of C sugar for export by way of their participation in the government regulated domestic market. The Complainants argue further that all the payments received for C sugar are on the export since C sugar is a product that must be exported. The European Communities responds that the benefits to the EC sugar industry from the EC sugar regime would exist regardless of the export of C sugar and are not contingent on the production or exportation of C sugar.

\(^{534}\) Appellate Body on Canada – Dairy (Article 21.5 – New Zealand and US II), para. 73.
\(^{535}\) See para. 7.238 above.
\(^{536}\) See also Section IV.D. of this Panel Report.
\(^{537}\) See paras. 4.44 and 4.51 above.
Assessment by the Panel

(i) The Panel's understanding of the EC sugar regime

7.244 Council Regulation (EC) No. 1260/2001 sets out rules to promote and protect the EC sugar industry. One main feature of the EC sugar regime is the establishment of price support for domestic sugar including intervention prices for sugar, supply controls by way of quotas, domestic market supply management, import restrictions and export subsidization. The EC sugar regime also sets out the basic price and the minimum price for beet, import and export licences, levies, export refunds; quotas and import restrictions; and preferential import arrangements.

7.245 The intervention price (minimum guaranteed price) for sugar is approximately three times the price of world market prices.\(^538\) The intervention price operates as a safety net that provides for intervention agencies to purchase EC quota sugar at a guaranteed price if sugar prices on the domestic market fall below a certain level. Intervention purchasing has occurred only once in 25 years\(^539\) as the regulatory aspects of the EC sugar regime controlling the amount of sugar sold in domestic markets and protection from outside competition enables quota sugar to be sold at prices well above the intervention price.

7.246 The EC Regulation provides rules for three different categories of sugar, i.e. A and B quota sugar and C sugar which is basically excess sugar. A, B and C sugar are produced, respectively, from A, B and C beet, the latter being used exclusively to produce C sugar.

7.247 A basic price for quota beet of standard quality\(^540\) is derived from the intervention price of white sugar and has been established at €47.67 per tonne.\(^541\) The Regulation also establishes minimum prices for A and B beet paid by A and B sugar producers to A and B beet growers. The minimum price of A beet has been set at €46.72 per tonne and that of B beet at €32.42 per tonne.\(^542\) Sugar producers are required to pay growers at least the minimum price for A and B beet they process into sugar. The price paid by the producers for C beet is generally lower than that paid for A and B beet.\(^543\) There is no regulated minimum price for C beet. However, because growers of C beet are also growers of A and B beet and because C beet can only be used in C sugar, which in turn belongs to the same production line as A and B quota sugar, the EC sugar regime ensures that the sale of under-priced C beet to C sugar producers is an integral part of the governmental regulation of the sugar market. Indeed, the production of C beet will depend on the needs of C sugar producers (since C beet can only be used in C sugar)\(^544\). Moreover, to be competitive C sugar must be exported at world price. Because of the low world price relative to C sugar cost of production, C sugar producers

\(^{538}\) The intervention price valid for standard quality sugar is €63.19/100 kg for white sugar and €52.37/100 kg for raw sugar. See Article 1 of Council Regulation (EC) No. 1260/2001.

\(^{539}\) Commission of the European Communities: Common Organisation of the Sugar Market Description, Exhibit COMP-8, p. 5.


\(^{544}\) The Panel is aware of the fact that strictly speaking there are no "C sugar producers" as such; there are no sugar producers that produce only C sugar. C sugar is produced by the producers of A and B sugar. Therefore "C sugar producers" are EC sugar producers who produce C sugar in addition to A and B sugar. The same is true for C beet. There are no sugar farmers who grow only C beet. C beet is grown by farmers of A and B beet. Therefore "C beet growers" are the EC beet farmers who also grow C beet, in addition to A and B beet. In the following section since the Panel examines the specific costs of growing or farming of C beet as well as the costs of production of C sugar, the Panel refers to C beet growers or farmers and C sugar producers with a view to emphasising the Panel's focus on C beet and C sugar.
exercise pressure on C beet growers so that C beet is sold to C sugar producers at reduced prices. Furthermore, various aspects of the sugar regime provide the beet growers with an incentive to produce beet beyond their A and B quota levels, as C beet. The discounted prices for C beet below its cost of production and the incentive for beet growers to produce C beet serve as an advantage for the export production of C sugar.

7.248 In accordance with Article 15 of the EC Regulation, a basic production levy is charged to manufacturers on their production of A and B sugar. The levy charged on A quota sugar is set at 2 per cent while the levy on B quota sugar is set at 37.5 per cent. These levies are used *inter alia* to fund export refunds given to exported A and B quota sugar under the co-financing principle of the EC sugar regime. The levies charged are split 42 per cent to sugar producers and 58 per cent to beet farmers.

7.249 The export refunds under the EC sugar regime cover the difference between the Community intervention price and the export price of EC quota sugar (that is world price). Export refunds are high, ranging from €443 per tonne of sugar for the 2001/2002 marketing year and €485 per tonne of white sugar for the 2002/3 marketing year. The export refund is well above the world price offered for exported quota sugar, which the EC Commission reports was €280 per tonne of white sugar in the marketing year 2001/02. Export refunds have been afforded to between 2.5 and 2.6 million tonnes of white sugar annually.

7.250 The high rate of export refunds to such a significant amount of exported sugar again adds to the revenues received by EC sugar producers from quota sugar sales, and may constitute one of the source of the spill-over effects of the EC sugar regime into the export production of C sugar.

(ii) Article 9.1(c) of the Agreement on Agriculture

7.251 In this dispute the Panel examines whether exports of C sugar are subsidized within the meaning of Article 9.1(c) of the *Agreement on Agriculture*. Article 9.1(c) requires the

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546 Commission of the European Communities: Common Organisation of the Sugar Market Description, Exhibit COMP-8, p. 13; levies only partially fund the export refunds for A and B quota sugar.
547 Commission of the European Communities: Common Organisation of the Sugar Market Description, Exhibit COMP-8, p. 13.
548 Commission of the European Communities: Common Organisation of the Sugar Market Description, Exhibit COMP-8, p. 20.
549 Commission of the European Communities: Common Organisation of the Sugar Market Description, Exhibit COMP-8, p. 20.
550 Commission of the European Communities: Common Organisation of the Sugar Market Description, Exhibit COMP-8, p. 20.
551 “Sugar in the European Union: sugar production costs and cross-subsidies to C sugar exports” by Roger Rose, Exhibit ALA-1, p. 4
552 Article 9.1(c) of the *Agreement on Agriculture* reads as follows:

Export Subsidy Commitments

1. The following export subsidies are subject to reduction commitments under this Agreement: (...)
   (c) payments on the export of an agricultural product that are financed by virtue of governmental action, whether or not a charge on the public account is involved, including
demonstration of three elements. First, it requires that "payments" be made. Second, that those payments be made "on the export of an agricultural product". And third, that those payments be "financed by virtue of governmental action".

7.252 The Complainants point to what they consider to be multiple "payments" which would be made "on export" and be "financed by virtue of governmental action." The Complainants submit that the EC sugar regime involves a series of payments including: (a) payment in the form of below costs C beet sales to C sugar producers/exporters; (b) payment in the form of cross-subsidization resulting from the profits made on sales of A and B sugar used to cover the fixed costs of the production/export of C sugar; (c) payment in the form of exports of C sugar below total costs of production; and (d) payments in the form of high prices paid by consumers.553

7.253 The Panel examines two of the payments (a) and (b) mentioned above. For each of the alleged payments, the Panel first examines whether there is indeed a payment. Then, the Panel discusses whether the alleged payments are "on export" and lastly, whether they are financed by virtue of governmental action.

(iii) Does the sale of C beet to C sugar producers constitute a payment on export financed by virtue of governmental action?

Is there a payment?

7.254 The Complainants argue that, as with milk as an input for the production of dairy products in Canada – Dairy, C beet, as the main input for the production of C sugar, is sold to C sugar producers/exporters at prices well below the total average cost of production of such C beet and, therefore, through this transaction provides C sugar producers with a payment-in-kind within the meaning of Article 9.1(c).

7.255 The European Communities does not deny that C beet is sold below the total average cost of beet growers but does not actually discuss whether sales of C beet to C sugar producers provide a payment-in-kind or a transfer of economic resources in favour of C sugar producers. In fact, the European Communities wrote in its first submission that "Canada – Dairy stands for the proposition that the provision of an agricultural input below its average total costs of production constitute a "payment" to the processor of that input."554 Although in response to a question by the Panel, the European Communities attempts to raise doubts on whether there is a sufficient "nexus", or degree of governmental action involved in the sales of C beet, the European Communities' main argument is that the matter is outside the Panel's terms of reference.555 The Panel has already dealt with the European Communities' procedural objection in paragraph 7.24 to 7.37, concluding that the parties arguments relating to C beet are within its terms of reference.

7.256 The Panel examines therefore whether the sales of C beet to producers of C sugar constitute a payment within the meaning of Article 9.1(c) of the Agreement on Agriculture.

7.257 As recognized by the Appellate Body in Canada – Dairy (Article 21.5 – New Zealand and US), Article 9.1(c) does not expressly identify any one criterion to be used in all situations of determining the existence of payment. The Appellate Body in that case established that an

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553 See for instance, Australia’s first written submission, para. 111-113 and Australia’s replies to Panel questions Nos. 46, 47 and 48; see also para. 4.39 above.

554 See paras. 7.3 and 7.18 above.
examination of whether a measure involves a payment must be determined on a case by case basis and by scrutinizing "the facts and circumstances of a disputed measure". 556 The Appellate Body decided there is no one benchmark that would apply to all situations and examinations of the existence of a subsidy. 557

7.258 In the first Canada – Dairy dispute, the Appellate Body concluded that "the word 'payments' [in 9.1(c)] embraces "payments-in-kind" and "specifically contemplates that the export subsidy may be granted in a form other than a money payment", "including revenue foregone". 560 Revenue or value may be foregone in instances when the price charged by the producer of the product is less than the product's proper value to the producer. In determining the proper value to the producer in assessing whether a transfer of economic resource has taken place, a "payment" analysis "requires a comparison between the price actually charged by the provider of the goods or services … and some objective standard or benchmark which reflects the proper value of the goods or services to their provider ... ". 561 The Appellate Body insisted that the standard to determine whether there is a transfer of economic resources must be objective and based on "the value of the milk" to the producer.

7.259 In looking for an appropriate benchmark to measure the proper value of commercially exported milk (CEM milk), the Appellate Body in Canada – Dairy (Article 21.5 – New Zealand and US) relied on the cost of production of such milk. The Appellate Body determined that if the producers of milk sell their milk below their total average cost of production, this loss must be financed from some other sources including by virtue of governmental action.

"Although the proceeds from sales at domestic or world market prices represent two possible measures of the value of milk to the producer, we do not see these as the only possible measures of this value. For any economic operator, the production of goods or services involves an investment of economic resources. In the case of a milk producer, production requires an investment in fixed assets, such as land, cattle and milking facilities, and an outlay to meet variable costs, such as labour, animal feed and health-care, power and administration. These fixed and variable costs are the total amount which the producer must spend in order to produce the milk and the total amount it must recoup, in the long-term, to avoid making losses. To the extent that the producer charges prices that do not recoup the total cost of production, over time, it sustains a loss which must be financed from some other source, possibly "by virtue of governmental action." (emphasis added)

7.260 For the Appellate Body, the average total cost of production takes best into account the "motivations of the independent economic operator who is making the alleged 'payments' and the value of milk to it." 563 If the sale is made at below the total cost of production of the domestic

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560 Appellate Body Report on Canada – Dairy, para. 112. Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US), para. 73. Later on in the US – FSC dispute, at para. 108, the Appellate Body clarified the use of the term "revenue forgone": "We held, in Canada – Milk, that "export subsidies" under the Agreement on Agriculture may involve, not only direct payments, but also "revenue forgone". We believe, however, that in disputes brought under the Agreement on Agriculture, just as in cases under Article 1.1(a)(i)(ii) of the SCM Agreement, it is only where a government foregoes revenues that are "otherwise due" that a "subsidy" may arise." Since we are in the present dispute referring to the fact that sales do not represent the proper value to producers, we will use the expression "value forgone".
producers of that product, there is a transfer of economic resources from the producers of the input product in favour of the processors/exporters of the said product. Hence, the Appellate Body concluded that the appropriate “benchmark” to determine the proper value of the milk was the average total cost of production of the subject milk. Hence, the objective standard for identifying the existence of payments focused on whether the CEM milk was priced at below the cost of its production.

7.261 In the present dispute, similar to that in Canada – Dairy (Article 21.5 – New Zealand and US), the Panel is examining whether the producers, here C beet growers, forego a portion of their proper value by way of the below total costs price charged to the producers of C sugar, or in other words whether C beet growers transfer economic resources, discounted C beet, in favour of C sugar producers/exporters.

7.262 In the Panel's view, the situation regarding the sale of milk to dairy processors in Canada – Dairy (Article 21.5 – New Zealand and US) is quite relevant and similar to the present matter. In that dispute, the issue was whether sales of CEM milk, served as a payment to Canadian dairy processors. The Appellate Body examined the industry-wide average total cost of production figure for milk and the price at which CEM milk was being sold by the milk producers to the processors. After determining the relevant costs and figures, it found that the price at which CEM milk was being sold to domestic dairy processors was well below the average total cost of production of such milk, that is below the proper value of CEM milk. The Appellate Body therefore concluded that the below cost of production sales of CEM involved payments on the export to Canadian dairy processors under Article 9.1(c) of the Agreement on Agriculture. The requirement that came along with the discounted purchase of CEM was that Canadian dairy processors incorporating CEM milk must, under Canadian law, export the resulting dairy product and divert it from the domestic market. Accordingly, the Appellate Body concluded that such transactions served as payment-in-kind and eventually an export subsidy under Article 9.1(c) of the Agreement on Agriculture by way of value foregone.

7.263 In the present dispute, the Complainants are arguing that, as in Canada – Dairy (Article 21.5 – New Zealand and US) and Canada – Dairy (Article 21.5 – New Zealand and US II), one of the types of payment allegedly being made in the EC sugar regime involves domestic inputs sold to sugar producers at prices that are below the total costs of production of beet growers. The Complainants argue that C beet (an input) is being sold to sugar producers at prices that do not remotely cover its cost of production.

7.264 The Panel is of the view that in the present dispute the total cost of production of C beet is an appropriate benchmark for determining whether the sales of C beet to C sugar producers provide a “payment” to the producers of C sugar within the meaning of Article 9.1(c) of the Agreement on Agriculture.

7.265 There is uncontested evidence that C beet is sold to C sugar producers at prices well below its cost of production, showing that the price received for C beet – calculated at 58 to 60 per cent of the price for C sugar – was below the total cost of production of that beet throughout the years 1992/93 to 2002/03. In particular, the Panel refers to the LMC Data, Datagro report "Considerations over
C sugar Production and Exports in the European Communities"569, the Report of the Netherlands Economic Institute "Evaluation of the Common Organization of the Markets in the Sugar Sector"570, Roger Rose's report "Sugar in the European Union; Sugar production costs and cross-subsidies to C sugar exports"571 and the Oxfam report "The Great EU Sugar Scam: How Europe's sugar regime is devastating livelihoods in the developing world".572

7.266 The average price received by farmers for C beet during that period ranged from *** to *** per cent of its average total cost of production.573 This means that, for at least the 11 most recent consecutive years, growers of beet failed to recover between *** and *** per cent of their total cost of producing C beet.

7.267 The European Communities does not contest the cost of production figures and related data offered by the Complainants. When specifically asked by the Panel for figures related to the cost of production, the European Communities refused, claiming that such figures were not related to its defence and that it did not find it necessary to express any views on the matter.574

7.268 As stated by the Appellate Body in EC – Hormones, "a prima facie case is one which in the absence of effective refutation by the defending party, requires a panel, as a matter of law, to rule in favour of the complaining party presenting the prima facie case."575 In the Panel's view, the uncontested evidence submitted by the Complainants demonstrates prima facie that C beet is sold at prices that do not cover its cost of production.

7.269 When C beet is sold to C sugar producers at rates that are below its total cost of production, there is, in effect, a payment, i.e. a payment-in-kind, being made to the C sugar producers to the extent that the proper value of C beet is not reflected in its price and, hence, involves a "payment" within the meaning of Article 9.1(c) of the Agreement on Agriculture by way of value foregone.

7.270 The Panel finds, therefore, that the below total cost of production sales of C beet to C sugar producers involves a payment within the meaning of Article 9.1(c) of the Agreement on Agriculture.

tonne of C sugar equivalent. In marketing year 1997/1998 the price of C beet per tonne of C sugar equivalent was ***, while its average total cost of production was *** per tonne of C sugar equivalent. In marketing year 1998/1999 the price of C beet per tonne of C sugar equivalent was ***, while its average total cost of production was *** per tonne of C sugar equivalent. In marketing year 1999/2000 the price of C beet per tonne of C sugar equivalent was ***, while its average total cost of production was *** per tonne of C sugar equivalent. In marketing year 2000/2001 the price of C beet per tonne of C sugar equivalent was ***, while its average total cost of production was *** per tonne of C sugar equivalent. In marketing year 2001/2002 the price of C beet per tonne of C sugar equivalent was ***, while its average total cost of production was *** per tonne of C sugar equivalent. In marketing year 2002/2003 the price of C beet per tonne of C sugar equivalent was ***, while its average total cost of production was *** per tonne of C sugar equivalent. The above figures are derived from the Datagro Report (Exhibit BRA-1, Table 5, p. 29). C beet prices are usually determined based on 58-60% of C sugar price. The prices set above are based on the high end estimates (60% of C sugar prices) that beet farmers may receive for C beet. See Commission of the European Communities: Common Organisation of the Sugar Market Description, Exhibit COMP-8, p. 10; NEI Report, Exhibit COMP-2, p. 160; Datagro Report, Exhibit BRA-1, p. 7.

568 LMC Data, Exhibit BRA-2, pp. 23 and 54
569 Datagro Report, Exhibit BRA-1, at pp. 5-7, and Table 5, p. 29.
570 NEI Report, Exhibit COMP-2, pp. 117-121 and 160.
571 "Sugar in the European Union: sugar production costs and cross-subsidies to C sugar exports" by Roger Rose, Exhibit ALA-1, pp. 1 and 8-12.
573 LMC Data, Exhibit BRA-2, Table 5.15, pp. 23 and 54; Datagro Report, Exhibit BRA-1, Table 5, Beet Farming Costs, p. 29.
574 European Communities' reply to Panel's question No. 32.
575 Appellate Body report on EC – Hormones, para. 104.
Is such payment-in-kind through sales of below-costs C beet made "on the export"?

7.271 The Complainants argue that since C beet can only be used in the processing of C sugar, which in turn must be exported, any payments received by C sugar producers are "on the export."  

7.272 The European Communities does not offer any specific arguments as to C beet and the issue of whether such payments to C sugar producers through below-costs-C beet are on the export. Instead, the European Communities focuses on the general argument in regard to C sugar (which encompasses C beet) that sugar producers are free to choose whether they want to produce C sugar for export. For the European Communities, even if the relevant EC measures provide an indirect benefit to C sugar, the governmental action which provides these benefits is not contingent upon the export of C sugar, since sugar producers may qualify for A and B quota rights and privileges regardless of whether they produce C sugar for export.

7.273 The Panel is of the view that the European Communities misinterprets the requirements of Article 9.1(c) with respect to 'on the export'. The European Communities focuses on the fact that C sugar production is not required under the EC Regulation and that the advantages received by sugar producers as a result of EC governmental action in regard to A and B sugar would be afforded whether or not they produce and export C sugar. But in the Panel's view, a payment "on export" does not need to be contingent upon export. An analysis of Article 9.1(c) would put its emphasis on whether the payment in question received is on the export, not on whether, as appears to be the case, the EC price support as a whole is de facto contingent upon C sugar being exported. In other words, when identifying whether a payment is on the export as defined under Article 9.1(c) of the Agreement on Agriculture, once a payment is identified, the focus is on whether this payment is made on the export, and not on whether the source of the payment is dependent or contingent on export production.

7.274 The Panel also recalls that in India – Autos the Panel dealt with the expression "on importation" which, in the Panel's view, has similarities with the expression "on export" with respect to the use of the term "on":

'The Panel turns therefore to consider the ordinary meaning of the phrase 'restriction…on importation'. An ordinary meaning of the term 'on', relevant to a description of the relationship which should exist between the measure and the importation of the product, includes 'with respect to', 'in connection, association or activity with or with regard to'. In the context of Article XI:1, the expression 'restriction…on importation' may thus be appropriately read as meaning a restriction 'with regard to' or 'in connection with' the importation of the product. On a plain reading, this would not necessarily be limited to measures which directly relate to the 'process' of importation. It might also encompass measures which otherwise relate to other aspects of the importation of the product.'

7.275 In the Panel's view a payment "on export" need not be "contingent" on export but rather should be "in connection" with exports.

7.276 The Panel considers that there is a very close link between C beet production and C sugar production, and in the Panel's view decisions by farmers of C beet whether or not to grow more C beet...
is essentially based on the needs of C sugar producers. The Panel recalls that C beet can only be used in C sugar. The Panel is aware that contrary to the situation for A and B beet, farmers and sugar producers are free to negotiate the price for C beet. Although EC Council Regulation No. 1260/2001 does not prescribe how much farmers should be paid for C beet, it is generally agreed in the intra-trade agreements between farmers and sugar producers that farmers receive about 60 per cent of the price that the sugar producers receive for C sugar. Indeed, contracts for C beet tend to follow the revenue sharing terms of A and B beet regulated contracts, with approximately 58-60 per cent of the C sugar price going to C beet growers and 42 per cent to sugar producers.

7.277 Sugar producers are free to decide whether or not to produce C sugar but once produced it must be exported unless it is carried forward to quota sugar for the following year (for a quantity up to a maximum of 20 per cent of A quota). Indeed, "C sugar not carried forward under Article 14 may not be disposed of on the Community's internal market and must be exported". Because C beet may be processed only into C sugar which in turn (unless carried forward as quota sugar as mentioned above) must be exported, payments by way of below cost of production sales of C beet to C sugar producers are "on the export". In other words, the payment by way of discounted C beet is only afforded to C sugar producers, and ultimately "on the export".

7.278 This is in line with the Canada – Dairy (Article 21.5 – New Zealand and US) case. The panel in that proceeding found that discounted CEM milk sold and used for dairy processing was available to processors only if CEM milk was used for exported dairy processing. Only by effectively exporting discounted CEM milk, in the form of processed dairy products, could producers gain access to the subsidized or discounted CEM milk. Accordingly, the panel, found that the payment through discounted milk to the dairy processors is made on the export. These panel findings were not appealed or otherwise modified by the Appellate Body.

7.279 The Panel finds, for the foregoing reasons, that the payments to C sugar producers by way of discounted below total cost of production sales of C beet by C beet growers are on the export within the meaning of Article 9.1(c) of the Agreement on Agriculture.

Is the payment-in-kind through sales of below-cost-C beet "financed by virtue of governmental action"?

7.280 The Complainants submit that the European Communities' governmental actions are indispensable to the transfer of resources described above. The European Communities' actions thereby finance growers to supply C beet to C sugar producers at prices that do not reflect the average total cost of production of the beet, and for those processors, in turn, to provide C sugar to buyers at

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582 A and B beet farmers are protected via minimum beet pricing or "basic beet price". The pricing system for beet establishes the minimum price at which sugar manufacturers may purchase sugar beet from EC farmers. This minimum price is set to at least 58 per cent of the intervention price (€366 per tonne of white sugar). The purpose of the beet (and cane) pricing arrangements is to ensure a stable and adequate income to beet farmers and a proper distribution of income throughout the sugar industry chain.
583 Commission of the European Communities: Common Organisation of the Sugar Market Description Exhibit COMP-8, p. 10; see also LMC Data, Exhibit BRA-2, pp. 15-16.
584 C sugar may be carried forward in a limited amount to the next marketing year to be estimated against the following years allocated quota under Article 14(1) of the EC Council Regulation No. 1260/2001.
world market prices that did not reflect its average total production cost. In its written submissions or oral statements the European Communities has not addressed this criteria *per se*.  

7.281 The Panel recalls that a "demonstrable link" and "clear nexus" between the "financing of the payments" and the "governmental action" must be established in order for the payment to qualify as a payment "by virtue of governmental action". The Appellate Body in *Canada – Dairy (Article 21.5 – New Zealand and US)* stated: "The words 'by virtue of' indicate that there must be a demonstrable link between the governmental action at issue and the financing of the payments, whereby the payments are, in some way, financed as a result of, or as a consequence of, the governmental action."  

7.282 The Appellate Body clarified the terms "financed by virtue of governmental action" in the second recourse on implementation in *Canada – Dairy (Article 21.5 – New Zealand and US II)*, when it stated:  

"As regards 'governmental action', we held in the first Article 21.5 proceedings that 'the text of Article 9.1(c) does not place any qualifications on the types of 'governmental action' which may be relevant under Article 9.1(c).' Instead, the provision gives but one example of governmental action that is 'included' in Article 9.1(c)—however, this example is merely illustrative. Accordingly, we stated that Article 9.1(c) 'embraces the full-range of activities by which governments 'regulate', 'control' or 'supervise' individuals'. In particular, we said that governmental action 'regulating the supply and price of milk in the domestic market' might be relevant 'action' under Article 9.1(c). Moreover, the governmental action may be a single act or omission, or a series of acts or omissions. We observe that Article 9.1(c) does not require that payments be financed by virtue of government 'mandate', or other 'direction'. Although the word 'action' certainly covers situations where government mandates or directs that payments be made, it also covers other situations where no such compulsion is involved.  

7.283 As the Panel discussed in paragraphs 7.247-7.248, the EC sugar regime regulates the prices at which A and B beet is sold to sugar producers. This is done to ensure a stable and adequate income to beet farmers and a proper distribution of income throughout the sugar industry chain. While Council Regulation No. 1260/2001 requires minimum payments to growers of A and B beet, it  

588 See paras. 4.70 to 4.86 to above.  
591 (footnote original) The example given is "payments that are financed from the proceeds of a levy imposed on the agricultural product concerned or on an agricultural product from which the exported product is derived".  
593 (footnote original) Ibid.  
594 (footnote original) Article 9.1(c) of the *Agreement on Agriculture* may be contrasted with Article 9.1(e) of the *Agreement on Agriculture*, as well as with Article 1.1(a)(i)(v) of the *SCM Agreement*, and items (c), (d), (j), and (k) of the Illustrative List of Export Subsidies (the "Illustrative List") of the *SCM Agreement*. In these provisions, some kind of government mandate, direction, or control is an element of a subsidy provided through a third party.  
596 Commission of the European Communities: Common Organisation of the Sugar Market Description, Exhibit COMP-8, p. 5.
permits processors to buy the beet they use to produce C sugar at prices below these minimums. However, because growers of C beet are also growers of A and B beet and because C beet can only be used in C sugar, which in turn belongs to the same production line as A and B quota sugar, the EC sugar regime ensures that the sale of under-priced C beet to C sugar producers is an integral part of the governmental regulation of the sugar market. Indeed, the production of C beet will depend on the needs of C sugar producers (since C beet can only be used in C sugar). Conversely, to be competitive, C sugar must be exported at the world price. Because of the low world price relative to C sugar costs of production, C sugar producers will exercise pressure on C beet growers so that C beet are sold to C sugar producers at reduced prices. As further detailed below, C beet growers can use the profits made on the sales of A and B beet to cross-subsidize the sale of C beet to C sugar producers at prices below the total costs of production of C beet while still making profits. C sugar producers will therefore be willing to pay C beet growers proportionally to what they receive on the sales of C sugar. There is evidence that indeed C beet growers usually receive some 60 per cent of the price of C sugar on the world market (as is the case with A and B beet). Again the EC Council Regulation, through its complete control over the production and sale of A and B sugar and A and B beet, controls and affects the production and sales conditions of C beet.

7.284 The Panel also notes that the EC Council Regulation No. 1260/2001 prescribes a framework for the contracts to be signed by beet growers and sugar processors. These contracts are known as inter-trade agreements. The prescriptions of the EC Council Regulation No. 1260/2001 provide therefore a minimum of protection for the farmer with respect to production and supply conditions (quotas, supply of seed, beet prices, delivery schedules, etc.) for which EC member States have a regulatory role. The actual intra-trade agreements are often more detailed than the EC sugar regime provides.

7.285 In answer to a Panel question, the European Communities submits that the availability and the cost of C beet may vary greatly between EC regions, as well as from one year to another, depending on a multiplicity of factors, which do not involve "government action", or at least the type of action at issue in this dispute. For example, the production of beet may be affected by climatic conditions and diseases to a much greater extent than the production of milk. Also, the European Communities argues that beet farmers are much less specialized than milk farmers. As a result, the production of C beet is as likely to be "financed" by A and B beet as by other alternative crops, and vice versa. The European Communities argues that what it describes as the "causal link" between the alleged "Government action" and the provision of C beet is not "tight" enough to consider that sales of C beet are "financed by virtue of Government action".

7.286 The Panel agrees with the Complainants that the European Communities does not provide any supporting evidence to substantiate its assertions in regard to causal links, such as what the income from alternative crops might be compared to income from price support for A and B beet, what those crops might be and whether such crops are also receiving governmental price support. Furthermore, evidence submitted shows that gross margins for C beet production in major C beet producing countries (i.e. France) is higher than the gross margin of alternative crops such as wheat. More importantly, the European Communities fails to explain why large numbers of EC farmers are engaged in growing C beet if such production only serves to deliver losses. Farmers make crop planting and livestock production decisions on the basis of expected prices and profits. Within a season, livestock and crop farmers will often cross-finance between different sectors, due to yield and price movements. This is as true for dairy cattle as for beet growing. However, the European Communities also fails to explain why farmers would maintain, within a mix of farming activities,
any sectoral production for which expected revenue is persistently less than the cost of production, in this case, production of C beet.

7.287 In the Panel's view, the Complainants have submitted prima facie evidence that C sugar producers provide positive incentives for growers to plan production above (the processor's) quota, by including an amount of C beet in a grower's beet delivery quota, at an average price, or paying a higher price of the first slice of over quota beet. As incentives, C sugar producers may cut next year's beet allocation for those growers who fail to meet the sugar producers' requirements, reallocating its delivery rights to more reliable growers.

7.288 The Panel recalls that C beet can only be used in C sugar. There is also evidence that C sugar producers have incentives to produce C sugar so as to maintain their share of the A and B quotas as well as the ability to profit from sales of C sugar even if the prices are below the total cost of production (fixed costs plus average variable costs). In the Panel's view, beet growers also have an incentive to plan production levels above A and B quota sugar requirements. C beet growers have an incentive to supply as much as is requested by C sugar producers with a view to receiving the high prices for A and B beet and their allocated amount of over-quota beet (or C beet). In this context, the Panel recalls that A, B and C beet are part of the same line of production, although the market for A and B beet – that is A and B quota sugar – is more lucrative than that of the C beet – that is C sugar. C beet producers can therefore sell below costs through the profits they make in selling A and B beet.

7.289 As noted by the Panel in paragraphs 7.261-7.263 above, there is a close similarity with the situation prevailing with CEM milk in Canada – Dairy (Article 21.5 New Zealand and US II) where the Appellate Body concluded that:

"where sales in the more remunerative market bear more than their relative proportion of shared fixed costs, sales in the other market do not need to cover their relative proportion of the shared fixed costs in order to be profitable. Rather, these sales can be made profitably below the average total cost of production. If the more remunerative sales cover all fixed costs, sales in the other market can be made profitably at any price above marginal cost. In these situations, the higher revenue sales effectively 'finance' a part of the lower revenue sales by funding the portion of the shared fixed costs attributable to the lower priced products. (...)"

7.290 The Panel recalls that since C beet can only be used in C sugar, the proportion of C beet production in relation to total beet production ought to correlate closely to the rate of C sugar production in proportion to total sugar production. Accordingly, since over the past years C sugar represents 11 to 21 per cent of the overall production of quota sugar, C beet must represent a similar level of total beet production in the European Communities. Hence, the growing of C beet is not incidental but rather an integral part of the governmental regulation of the sugar market.

7.291 The Panel is of the view that a significant percentage of farmers of C beet are likely to finance sales of C beet below the costs of production as a result of participation in the domestic market in selling high priced A and B beet. The Panel considers that, through EC Council Regulation No. 1260/2001, the European Communities controls virtually every aspect of domestic beet and sugar supply and management. In particular, the EC Regulation fixes the price of A and B beet that renders

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600 See NEI Report, Exhibit COMP-2, pp. 159-164 for discussion on the incentives and intentional farming of C beet.
it highly remunerative to farmers/growers of C beet. Government action also controls the supply of A
and B beet (and sugar) through quotas. The imposition by government of financial penalties on
producers of C sugar that divert C sugar into the domestic market is another element of governmental
control over the supply of beet and sugar. Further, the degree of government control over the
domestic market is emphasized by the fact that the EC Sugar Management Committee oversees,
supervises and protects the EC domestic sugar through, *inter alia*, supply management.604 In sum, the
European Communities controls both the supply and the price of sugar in the internal market. This
controlling governmental action is "indispensable" to the transfer of resources from consumers and
tax payers to sugar producers for A and B quota sugar and, through them, to growers for A and B
quota beet.605

7.292 The Panel finds, for the foregoing reasons, that C sugar producers receive payments on export
*financed by virtue of governmental action* through various governmental actions as specified above,
within the meaning of Article 9.1(c) of the *Agreement on Agriculture*.

**Conclusion**

7.293 Therefore, the Panel finds that C sugar producers receive payment on export by virtue of
governmental action through sales of C beet below the total costs of production to C sugar producers.
Pursuant to Article 10.3 of the *Agreement on Agriculture*, the Panel finds that the European
Communities has not demonstrated that exports of C sugar that exceed the European Communities' commitment levels since 1995 and in particular since the marketing year 2000/2001, have not been subsidized. Consequently, the European Communities is acting inconsistently with Articles 3 and 8 of the *Agreement on Agriculture*.

(iv) **Does the cross-subsidization resulting from the EC sugar regime constitute a payment on exports by virtue of governmental action?**

7.294 The Panel notes, in analyzing the alleged payments in this case, that there is an intellectual challenge stemming from the fact that the producers of A, B and C sugar are the same companies and that the production of all three classifications of sugar is made in a continuous line of production. Were the producers of C sugar different from those of A and B sugar, and were they receiving "economic resources" from the producers of A and B sugar in order to produce C sugar, the analysis would appear more straightforward. The Panel also notes that any alleged payments in the production of sugar, wherever they take place, derive from the high prices paid for A and B quota sugar on the EC domestic market. For these reasons, the Panel concentrates its analysis of C sugar on the issue of cross-subsidization.

7.295 The Complainants submit that the advantages that exporters of C sugar receive through the transfer of economic resources that result from the EC sugar regime (which allows them to produce and export C sugar at above average variable cost but below average total cost of production) are payments. The Complainants argue that the EC sugar regime's combination of guaranteed intervention prices, production quotas, export refunds and import restraints all limit the quantity of quota sugar that may be sold in the internal market and directly results in the high domestic prices for A and B quota sugar. The Complainants also argue that the EC sugar regime and the high administered above-intervention price paid for domestic EC sugar result in an eventual payment to EC sugar exporters within the meaning of Article 9.1(c).606 Specifically, they submit that the high

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605 Appellate Body Report on *Canada – Dairy*, para. 120.
606 Brazil’s first written submission, para. 45.
prices result in covering the fixed costs to produce the exported C sugar, hence, serving as a subsidy to C sugar producers.\footnote{607}

7.296 The European Communities argues that some of the measures cited by the Complainants, such as import tariffs or safeguard measures, are not subsidies. Other measures, such as the intervention price and the production quotas, are indeed typical domestic price support mechanisms, and are already subject to the European Communities' domestic support reduction commitments under the Agreement on Agriculture. Therefore, the question of whether these measures provided export subsidies to C sugar does not even arise.

7.297 The Panel acknowledges, as was stated by the Appellate Body in \textit{Canada – Dairy (Article 21.5 – New Zealand and US)}, that normal economic operators must cover their total costs of production and if they do not, this may be evidence that they receive an advantage of some sort:

'For any economic operator, the production of goods or services involves an investment of economic resources. In the case of a milk producer, production requires an investment in fixed assets, such as land, cattle and milking facilities, and an outlay to meet variable costs, such as labour, animal feed and health-care, power and administration. These fixed and variable costs are the total amount which the producer must spend in order to produce the milk and the total amount it must recoup, in the long-term, to avoid making losses. To the extent that the producer charges prices that do not recoup the total cost of production, over time, it sustains a loss which must be financed from some other source, possibly "by virtue of governmental action".\footnote{608}

7.298 The Panel recalls that in the ordinary course of business, a private business or economic operator would make the decision to produce and sell a product, not only to recover the total cost of production, but also with the objective of making profits. The Panel is of the view that export sales below total cost of production cannot be sustained unless they are financed from some other source, possibly "by virtue of governmental action".\footnote{609}

7.299 The Panel recalls that the Appellate Body in \textit{Canada – Dairy (Article 21.5 – New Zealand and US)} determined that the appropriate "benchmark" to assess the proper value of the subject good, considering the facts and circumstances of the dispute, was the average total cost of production of the CEM milk. In determining the proper value to the producer, a payment analysis "requires a comparison between the price actually charged by the provider of the goods or services ... and some objective standard or benchmark which reflects the proper value of the goods or services to their provider...".\footnote{610} In that dispute the Appellate Body, in search of an objective standard that would establish the proper value of milk to the milk producer, found that the average total cost of production took best into account the "motivations of the independent economic operator who is making the alleged 'payments'" and the value of milk to it.\footnote{611} The Appellate Body used this benchmark as it answered the "crucial question, namely, whether Canadian export production has been given an advantage."\footnote{612} (emphasis added)

\footnote{607}{The Complainants submit that the subsidy, as defined in Article 9.1(c) of the Agreement on Agriculture, takes shape by way of the coverage of costs serving as a payment on exports which is the result of financing by governmental action.}
\footnote{608}{Appellate Body Report on \textit{Canada – Dairy (Article 21.5 – New Zealand and US)}, para. 87.}
\footnote{609}{Appellate Body Report on \textit{Canada – Dairy (Article 21.5 – New Zealand and US)}, para. 87.}
\footnote{610}{Appellate Body Report on \textit{Canada – Dairy (Article 21.5 – New Zealand and US)}, para. 74.}
\footnote{611}{Appellate Body Report on \textit{Canada – Dairy (Article 21.5 – New Zealand and US)}, para. 92.}
\footnote{612}{Appellate Body Report on \textit{Canada – Dairy (Article 21.5 – New Zealand and US)}, para. 84.}
The Panel recalls that the Appellate Body in Canada – Dairy (Article 21.5 – New Zealand and US) looked at why dairy farmers could make such below cost of production sales, and why they were able to do so without making a loss, indeed while making a profit. In reviewing the Canadian dairy regime the Appellate Body found that profits from domestic milk were spilling over to allow the sale of CEM milk at discounted prices – through governmental price controls. 

The evidence submitted shows that C sugar prices have been well under its average total cost of production every year, from 1992/1993 to 2002/2003. In marketing year 2000/2001, the price per tonne of C sugar, based on the London Daily Price, was €222.32, while the total cost of production for that sugar was *** per tonne. This data illustrates that the price charged for C sugar does not even remotely cover its cost of production.

Referring to publicly available information, the European Communities considers that, as a general rule, sugar producers operate at a profit. In the Panel's view, profits are only possible if

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614 Datagro Report, Exhibit BRA-1, Table 5, p.29 and Table B-15; "Sugar in the European Union: sugar production costs and cross-subsidies to C sugar exports" by Roger Rose, Exhibit ALA-1, pp. 8-10; LMC Data, Exhibit BRA-2, Table 5.15, p. 54; Oxfam Briefing Paper 27, August 2002. Exhibit COMP-3, pp. 1, 8-9; EC Court of Auditors Special Report No 20/2000, Exhibit COMP-1, p. 35; NEI Report, Exhibit COMP-2, Table 7.3, p. 113.
615 The London Daily Price is a spot price for EC sugar and, hence, may represent a more accurate indication of the premium that EC sugar receives. See LMC Data, Exhibit BRA-2, p. 23.
616 Ibid.
617 In marketing year 1995/1996 the price per tonne of C sugar was ///, while total cost of production for that sugar was *** per tonne. In marketing year 1996/1997 the price per tonne of C sugar was ///, while total cost of production for that sugar was *** per tonne. In marketing year 1997/1998 the price per tonne of C sugar was ///, while total cost of production of that sugar was *** per tonne. In marketing year 1998/1999 the price per tonne of C sugar was ///, while total cost of production of that sugar was *** per tonne. In marketing year 1999/2000 the price per tonne of C sugar was ///, while total cost of production of that sugar was *** per tonne. In marketing year 2000/2001 the price per tonne of C sugar was /// while total cost of production of that sugar was *** per tonne. In 2002/2003 the price per tonne of C sugar was /// while the total cost of production for that sugar was *** per tonne. See Datagro Report, Exhibit BRA-1, Table B. 15.
618 The EC has not contested the Complainants' evidence that C sugar is sold at prices that give the producers a positive contribution to net income even though those prices are approximately *** per cent below average total cost of production. Accordingly, the evidence clearly establishes that a "significant proportion" of EC producers –and one hundred per cent of those producing C sugar – make export sales of C sugar at prices below the average total cost of production.
619 European Communities' reply to Panel question 68. The Panel also notes the non-refuted evidence submitted by the Complainants. Most, if not all, of EC sugar producers operate on a profitable basis, particularly those companies that operate in the relatively more efficient C sugar producing regions. [For example, reported profits for 2002-03 were €31 million and €315 million for Royal Cosun and Sudzucker, respectively (a substantial part of Sudzucker's profit would have been earned through its 85 per cent equity in St Louis Sucre). In the same year, Danisco reported a profit of DKK1017 million. (€139 million). The Associated British Foods group that includes British Sugar as a subsidiary reported a profit of £176 (€264 million). According to the Financial Times (15 April 2004, p.24) profits for the Associated British Foods subsidiary appears likely to be higher in 2003-04 than in 2002-03, with high sugar yields accounting for much of an increase in profit for the first half of the year from £73 million to £85 million. In 2002-03 St Louis Sucre's profit was €132 million. The most representative measure of return to capital available on a common basis is the return to shareholders' funds. Profit as a percentage of shareholders funds for 2002-03 was 6.4, 14.2, 7.5 and 36.2 for Royal Cosun, Sudzucker, Danisco and St Louis Sucre, respectively. To the extent that the value of sugar quotas is included in the reported value of capital, these figures will underestimate the true contribution of quota sugar profits to rates of return. Only for St Louis Sucre is the issue addressed specifically for sugar quotas in the accounts. There, it is stated that the value of sugar quotas purchased in company amalgamations is amortised over 20 years.]
C sugar is being sold above average variable costs despite being sold below its average total cost of production and its fixed costs are financed through some other way.

7.303 In the Panel's view, payments could occur by virtue of a combination of factors and measures. The Complainants have submitted extensive evidence and argumentation as to why and how cross-subsidization occurs within the EC sugar regime.\textsuperscript{620} From the uncontested evidence, the Panel understands that the European Communities controls the supply of sugar within the European Communities which has a direct impact on the price of sugar in the domestic market; indeed prices of A and B sugar are three times higher than the world market price.\textsuperscript{621} The primary measures are controls on the supply of sugar to the domestic market (including restrictions on sales into the domestic market, import quotas and requirements to export designated quantities of sugar) and direct subsidies for production and export, with intervention buying as a fallback should the sugar price fall to the intervention price. While there are no controls on the quantities of C sugar that may be produced and exported, penalties attach to such sugar if it is not exported or otherwise carried forward. In addition, EC controls on alternative sweeteners, such as isoglucose, serve to negate competition from more competitively priced products.

7.304 The Panel recalls that the quantities of sugar that may be sold on the domestic market are tightly regulated through import controls and controls on the quantities of domestically produced sugar that may be disposed of within the European Communities, together with subsidized exports, as a key supply management mechanism designed to avoid intervention buying.

7.305 The EC regime\textsuperscript{622} includes mechanisms designed to regulate the domestic supply of sugar produced from EC-harvested beet or cane. The main instrument is the system of categorization of such sugar into A and B quotas and C sugar (surplus to quota). Sugar produced as quota or as C sugar is reclassifiable under certain circumstances under EC regulatory arrangements. The A quota sugar (which comprises around 82 per cent of the total quota) is the more valuable quota and is nominally intended to meet domestic demand.\textsuperscript{623} The regime provides for annual A and B sugar production quotas for each member State, established for a five-year period. Member States are responsible for assigning the quotas to sugar producers. The quotas constitute the maximum quantities eligible for domestic price support and direct export subsidies (in EC terminology, 'refunds'). There is no limit on sugar production above A and B quota but such excess sugar (C sugar) has to be exported if not carried forward. Penalties are provided for when export sugar surplus to A and B quota sugar (C sugar) is not exported. However, as member States are authorized to reduce quotas, failure to produce up to maximum quota levels could lead to reductions in the quotas assigned to individual processors.

7.306 There are no limits on the quantity of C sugar that may be produced or exported, but such sugar cannot be sold on the domestic market and it is not eligible for intervention or export refunds. There is no independent production of C sugar. The manufacture of quota and non-quota sugar is undertaken by the same enterprises. There is nothing in the regime to prevent producers pooling subsidies for quota sugar to average out subsidies and charges over total sugar production.\textsuperscript{624} In fact,

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\textsuperscript{621} See LMC Data, Exhibit BRA-2, Table 3.4, p. 22; and Datagro Report, Exhibit BRA-1, Table 8.15 and Table 5, p. 29.

\textsuperscript{622} See also Factual Aspects in Section III above.

\textsuperscript{623} Commission of the European Communities: Common Organisation of the Sugar Market Description, Exhibit COMP-8, p. 9.

\textsuperscript{624} In 1981, the EC advised a GATT working party: "... that the sugar regime resulted in the pooling of producers receipts from sales in the internal markets at supported prices, receipts, from exports of B quota sugar
the EC regime is predicated on a single stream of manufacture of quota and non-quota sugar by sugar quota holders, given that quota and non-quota sugar are reclassifiable to a certain extent and given also the conditionality attached to the grant of an export certificate for C sugar. As acknowledged by the EC Commission, the production of C sugar is directly linked to quota production. 

7.307 Important by-products of this production support are structural surpluses, with EC sugar production substantially in excess of consumption. Consumption averages around 12.5 million tonnes, whereas production ranges between 15-18 million tonnes. In addition to sugar manufactured from domestically harvested beet or cane, a further 1.8 million tonnes of sugar is manufactured from raw cane sugar imported mainly from the ACP countries. The regime ensures that domestic production surplus to consumption is disposed of on export markets. Approximately 20 per cent of all sugar produced is exported.

7.308 Export subsidies are funded by producer levies, calculated on the basis of quota production by sugar producers. The EC Commission awards export subsidies through Management Committee procedures. Export refunds/subsidies to A and B quota sugar may be fixed at regular intervals or by a tender system the proceeds of which cover the difference between the EC domestic sugar price and the world market price for sugar, hence, enabling EC sugar to be exported and sold on the world market. The export refund amounts are significant which indicates that the EC sugar industry needs a great deal of support or subsidies to competitively sell sugar on the world market.

7.309 When EC consumers pay the regulated high price for domestic sugar (A and B quota sugar), these domestic transactions generate substantial financial resources and constitute an "advantage" to the same producers in their production of C sugar.

7.310 The Panel finds that there is clear evidence that the relatively high EC administered domestic market (above-intervention) prices for A and B quota sugar allow the sugar producers to recover fixed costs and to sell exported C sugar over average variable costs but below the average total cost of production. Sugar is sugar whether or not produced under an EC created designation of A, B or C sugar. A, B or C sugar are part of the same line of production and thus to the extent that the fixed costs of A, B and C are largely paid for by the profits made on sales of A and B sugar, the EC sugar regime provides the advantage which allows EC sugar producers to produce and export C sugar at below total cost of production. For the Panel this cross-subsidization constitutes a payment in the form of a transfer of financial resources.

7.311 The European Communities submitted that, despite the fact that a party derives an "advantage" from certain "governmental actions", it does not follow necessarily that any provision of goods made by that party would "transfer economic resources" to the recipient of the goods. The European Communities contends that the "benefit" had to be examined on its own merits, and under the relevant WTO rules. In the European Communities' view, by de-linking the "benefit" from the "payment" and attaching it to the "governmental action", the Complainants' interpretation of Article 9.1(c) would extend the application of the strict rules on export subsidies provided in the Agreement on Agriculture to virtually any form of government intervention which might have the...
incidental effect of "financing" sales at a loss. According to the European Communities, this was never intended by the drafters of the *Agreement on Agriculture*.

7.312 The Panel is of the view that Article 9.1(c) of the *Agreement on Agriculture* does not require the demonstration of a benefit for a measure to constitute a payment within Article 9.1(c) of the *Agreement on Agriculture*. The special nature of Article 9.1(c) is such that once an advantage or payment has been demonstrated, there is no need to prove separately that such an advantage provide "benefits" to the producers. The only additional requirements are that the advantage or payment is on export and is financed by virtue of governmental action.

7.313 Finally, to the European Communities' argument that several of the measures identified by the Complainants are not subsidies but rather tariffs and other types of border measures, the Panel recalls that in *Canada – Dairy (Article 21.5 – New Zealand and US II)*, the Appellate Body stated that governmental action, within the meaning of Article 9.1(c) embrace a full-range of activities by governments and that governmental action may be a single act or omission, or a series of acts or omissions.630

7.314 The Panel finds therefore that the cross-subsidization taking place through the cumulative effect of various measures involved in the operation of the EC sugar regime, including high prices charged to domestic consumers, enables C sugar producers to produce and sell C sugar. In the Panel's view, there is a payment in the form of transfers of financial resources from the high revenues resulting from sales of A and B sugar, for the export production of C sugar, within the meaning of Article 9.1(c) of the *Agreement on Agriculture*.

**Is the payment on export?**

7.315 The Complainants contended that the payments made to C sugar producers were payments "on the export" of "an agricultural product" within the meaning of Article 9.1(c) of the *Agreement on Agriculture*.

7.316 For the European Communities, even if these measures provided an indirect benefit to C sugar, they were not contingent upon the export of C sugar and, therefore, could not be characterized as "export subsidies". The European Communities argued that a sugar producer's eligibility for A and B production quotas did not depend on whether it exported any sugar. Likewise, the right to sell A and B sugar into intervention was not conditional upon whether it exported C sugar or indeed any sugar at all. In this regard, the European Communities noted that some sugar producers did not produce any C sugar at all. The European Communities noted further that according to data for the most recent marketing year, there were no exports of C sugar from Italy, Greece and Portugal, while exports from Finland, Spain and Belgium/Luxemburg represented only a fraction of their total sugar output.

7.317 As discussed before, an analysis of Article 9.1(c) shows that the focus of the analysis is on whether the payment received is "on the export" or provides an advantage to the exports, not whether the whole EC regime, or the cross-benefits resulting from A and B quotas are contingent upon C sugar being exported.

7.318 The Panel recalls that C sugar, unless carried forward, must be exported, whether it is exported by the C sugar producer or any other intermediary. The European Communities admits that

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whether C sugar is exported by C sugar producers or some other intermediate is of no relevance; what matters is that C sugar must be exported.\textsuperscript{631}

7.319 Moreover, the Panel notes that the European Communities has not disputed that \textit{all} companies that produce C sugar participate in the domestic market through production of A or B sugar, or both. In \textit{Canada – Dairy (Article 21.5 – New Zealand and US II)} the Appellate Body held that it was irrelevant that some producers did not make payments within the meaning of Article 9.1(c) of the \textit{Agreement on Agriculture}. It found that Canada would still act inconsistently with its export subsidy commitments even if some producers never make or participate in the discounted sales. The requirement is not that every single producer be involved in receiving or transferring payments but rather that the system provides for or even encourages such an occurrence.\textsuperscript{632}

7.320 The Panel is of the view that such an occurrence is not, as suggested by the European Communities, a mere “incidental effect” of financing below cost of production of C sugar exports. The Panel fails to see a mere “incidental effect” in view of the great discrepancy between the cost of production and the C sugar prices. For instance, the evidence submitted shows that for 2000/2001 C sugar was priced at €222.39 per tonne. But the total cost of production for that same sugar in that marketing year was on average *** per tonne.\textsuperscript{633} The evidence submitted also shows that for 2001/2002 C sugar was priced at *** per tonne. But the total cost of production for that same sugar in that year was on average *** per tonne.\textsuperscript{634} Nobody could consider the effects of a product paying for only *** per cent of its total cost of production in 2000/2001 and *** per cent of its total cost of production in 2001/2002, or at *** and *** below its cost of production, respectively, as “incidental”. Moreover there is evidence that production of C sugar represents some 11-21 per cent of the total EC sugar production.\textsuperscript{635}

7.321 The Panel recalls that C sugar could only be sold for export. If not reclassified, C sugar “may not be disposed of in the Community's internal market and must be exported without further processing.”\textsuperscript{636} Because of that legal requirement, advantages, payments or subsidies to C sugar, that must be exported, are subsidies “on the export” of that product. It seems clear that if the producer had a choice to either sell on the EC domestic market or on the world market, the former would be more attractive, given that the EC regime delivered a domestic price of some 3.5 times the world price of A quota sugar and 2.5 times that of B quota sugar.\textsuperscript{637} The only reason why producers of C sugar export C sugar, is because they are prohibited from introducing such sugar into the domestic market, facing heavy penalties pursuant to Article 13 of the EC Regulation if they do. They decide to produce C sugar because they are able to export it at prices above its average variable costs after covering a portion of the fixed costs by way of spill-over from sales of A and B sugar.

7.322 The Panel finds that the payment on C sugar production in the form of transfer of financial resources through cross-subsidization resulting from the operation of the EC sugar regime is \textit{on export} within the meaning of Article 9.1(c) of the \textit{Agreement on Agriculture}.

\textsuperscript{631} European Communities’ reply to Panel question No. 62(b): "However, no meaningful distinction can be made between the export sales made directly by the sugar companies and those made through trading companies. The C sugar sold to the traders cannot be resold within the EC. Further, in both cases the sugar is usually delivered by the sugar companies FOB at an EC port. Moreover, sometimes the trading companies are not even established in the EC. Thus, for all practical purposes, sales of C sugar to traders are export sales, just like the export sales made directly by the sugar companies.”


\textsuperscript{633} Datagro Report, Exhibit BRA-1, Table B.15 and Exhibit ALA-1, table 2 on page 8.

\textsuperscript{634} Datagro Report, Exhibit BRA-1, Table B.15.

\textsuperscript{635} EC Commission Court of Auditors, Special Report No 9/2003, Exhibit COMP-11, p. 23, para. 38.

\textsuperscript{636} Articles 13(1) of EC Council Regulation No. 1260/2001

\textsuperscript{637} See LMC Data, Exhibit BRA-1, Table 3.4, p. 22; and Datagro Report, Exhibit BRA-1, Table B.15 and Table 5, p. 29.
Is this cross-subsidization payment financed by virtue of governmental action?

7.323 The Complainants submit that as in Canada – Dairy, the controlling governmental actions are "indispensable" to the transfer of resources from consumers and tax payers to sugar processors for A and B quota sugar and, through them, to growers of A and B quota beet.\footnote{Appellate Body Report on Canada – Dairy, para. 120.}

7.324 The Panel recalls that the "demonstrable link" and clear "nexus" between the "financing of payments" and the "governmental action" must be established in order to qualify as a payment "by virtue of governmental action."\footnote{Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US II), para. 130; see also Appellate Body Report, Canada – Dairy (Article 21.5 – New Zealand and US), para. 113.} In Canada – Dairy (Article 21.5 – New Zealand and US II), the Appellate Body stated that "Article 9.1(c) "embraces the full-range' of activities by which governments 'regulate', 'control' or 'supervise' individuals'.\footnote{(footnote original) Appellate Body Report, Canada – Dairy (Article 21.5 – New Zealand and US), para. 112.} In particular, it said that governmental action 'regulating the supply and price of milk in the domestic market' might be relevant ‘action’ under Article 9.1(c).\footnote{(footnote original) Ibid.} It added that "Article 9.1(c) does not require that payments be financed by virtue of government 'mandate', or other 'direction'. Although the word 'action' certainly covers situations where government mandates or directs that payments be made, it also covers other situations where no such compulsion is involved.\footnote{Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US II), paras. 127 and 128.}

7.325 Of particular relevance in the present dispute is the Appellate Body's discussion of the word "financed" (by virtue of governmental action) which refers to the "mechanism or process" put in place by the government: The word refers generally to the mechanism or process by which financial resources are provided to enable 'payments' to be made.\footnote{Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US II), para. 132.}

7.326 The Panel considers that the European Communities' governmental action regulating the domestic sugar market cross-subsidizes sales of C sugar that otherwise would not be made, or would be made at a loss. The higher revenue sales for quota sugar in the internal market effectively finances some or all of the fixed costs of C sugar. C sugar is cross-subsidized through direct subsidies, price support mechanisms and related mechanisms for quota sugar, all of which are regulatory instruments of the EC sugar regime. The sales of C sugar are profitable at prices that merely exceed average variable costs because the higher revenue sales of A and B quota sugar in the internal market "effectively financed part of the lower revenue sales by funding the portion of the shared fixed costs attributable to the lower priced products."\footnote{Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US), paras. 139-140.}

7.327 With respect to market access, the European Communities recalled that the terms "governmental action" in Article 9.1(c) encompass a broad range of government measures,\footnote{Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US II), para. 144.} including import tariffs.\footnote{Appellate Body Report on Canada – Dairy (Article 21.5 – New Zealand and US II), para. 144.} The Complainants' interpretation would imply that, if high import duties had the incidental effect of "cross-financing" exports below the average total cost of production, the...
Member concerned would have no alternative but to lower its import duty levels, even if such duties were within that Member's tariff bindings.

7.328 The Panel is of the view that the production of C sugar is not incidental. The Panel recalls that there are no independent producers producing exclusively C sugar: C sugar production exists only for producers of A and B quota sugar. The EC sugar regime provides the incentive to EC sugar producers to produce C sugar. This incentive lies in the fact that under the EC sugar regime if all the allocated quota for A and B sugar is not satisfied by the producer, the producer runs the risk that the quota will be reallocated to another sugar producer. There is evidence that C sugar was initially intended to secure the full quota for a given year and should amount to approximately 6 per cent of quota production. Yet, the EC Court of Auditors have stated that, over the past years, C sugar production has varied between 11 and 21 per cent of quota production. The evidence demonstrates that one reason for this excessive production of C sugar is that the spill-over of profits from sales of A and B quota sugar allows C sugar fixed costs to be covered and, hence, allows it to be sold profitably above its average variable costs. This is further evidence of the advantage provided to C sugar producers. Otherwise, C sugar would not be produced at such levels if it were only to ensure satisfaction of quota allocation.

7.329 The Panel recalls that the Appellate Body stated that the use of WTO-consistent domestic support cannot be without limits:

"However, we consider that the distinction between the domestic support and export subsidies disciplines in the Agreement on Agriculture would also be eroded if a WTO Member were entitled to use domestic support, without limit, to provide support for exports of agricultural products. Broadly stated, domestic support provisions of that Agreement, coupled with high levels of tariff protection, allow extensive support to producers, as compared with the limitations imposed through the export subsidies disciplines. Consequently, if domestic support could be used, without limit, to provide support for exports, it would undermine the benefits intended to accrue through a WTO Member's export subsidy commitments."

7.330 In the Panel's view, the EC sugar regime is such that it creates incentives to breach the ordinary limits of domestic support by encouraging producers to produce more sugar for export in order to ensure they fulfil their quotas and prevent them from losing access to the preferential quotas. More importantly though, by virtue of the high prices charged to domestic consumers and the operation of the A and B quotas as well as other features of the EC sugar regime, exporters of C sugar can cover a significant portion of their production costs and make profitable export sales.

7.331 The Panel is thus of the view that EC sugar producers finance sales of C sugar at below cost of production directly by participating in the domestic market and making sales internally at high prices as regulated by the European Communities (and from the purchase of discounted C beet as discussed earlier). The European Communities' governmental action controls virtually all aspects of domestic sugar supply and pricing. The European Communities provides this control through a combination of guaranteed intervention prices, production quotas and import restraints which limit the quantity of quota sugar that may be sold in the internal market, and the resulting high domestic price for A and B quota sugar. The domestic sales offer lucrative and attractive returns to producers. Government action controls the supply of domestic sugar by way of quotas in pursuit of protecting

648 NEI Report, Exhibit COMP-2, p. 117.
650 NEI Report, Exhibit COMP-2, pp. 117 and 160.
high domestic prices well above the intervention price. Additionally, penalties levied against sugar producers that divert C sugar production into the domestic market are evidence of further governmental control. The collection of production levies and distribution of export refunds also contribute to the high degree of EC governmental control. Lastly, the imposition of high import tariffs illustrates again governmental action in the EC sugar regime.

Accordingly, the EC sugar regime uses the high profits on A and B quota sugar to cover fixed costs for C sugar and, most importantly, requires C sugar to be exported and diverted from the domestic market. Again, the result of the EC sugar system is not the production of C sugar in marginal or superfluous amounts simply in the pursuit of ensuring quota fulfilment. Rather, as the EC Court of Auditors stated, over the past years, C production has varied between 11 and 21 per cent of quota production, a significant portion of the European Communities' entire sugar production.

In the Panel's view, the EC sugar regime and the cross-over benefits that it creates are thus the direct and foreseeable consequences of actions by the European Communities, within the meaning of Article 9.1(c) of the Agreement on Agriculture, not merely the decisions of private sugar producers responding to market incentives.

Therefore, the Panel finds that the production of C sugar receives a payment, through cross-subsidization resulting from the operation of the EC sugar regime: there is a payment, in the form of transfers of financial resources on export financed by virtue of governmental action.

Pursuant to Article 10.3 of the Agreement on Agriculture, the Panel finds that the European Communities has not demonstrated that exports of C sugar that exceed the European Communities' commitment levels since 1995 and in particular since the marketing year 2000/2001, are not subsidized. Consequently, the European Communities is acting inconsistently with Articles 3 and 8 of the Agreement on Agriculture.

5. Overall conclusion

The Complainants have provided prima facie evidence that the European Communities' exports of sugar exceeds its commitment levels since 1995 and in particular since the marketing year 2000/2001.

The Complainants have also provided prima facie evidence that producers/exporters of ACP/India equivalent sugar that exceed the European Communities' commitment levels receive subsidies within the meaning of Article 9.1(a) of the Agreement on Agriculture.

The Complainants have provided prima facie evidence that producers/exporters of C sugar that exceed the European Communities' commitment levels receive payments on export by virtue of governmental action: (i) through sales of C beet to C sugar producers below their total costs of production; and (ii) in the form of transfers of financial resources, through cross-subsidization resulting from the operation of the EC sugar regime, within the meaning of Article 9.1(c) of the Agreement on Agriculture.

In light of Article 10.3 of the Agreement on Agriculture, the Panel reaches the conclusion that the European Communities has not demonstrated that its exports of C sugar and ACP/India (equivalent) sugar that exceed the European Communities' commitment level are not subsidized.

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652 LMC Data, Exhibit BRA-1, Tables 3.1-3.4, pp. 18-22 and Exhibit ALA-1.
Consequently, the Panel finds that the European Communities has been acting inconsistently with its obligations under Articles 3.3 and 8 of the Agreement on Agriculture by providing export subsidies on sugar within the meaning of Articles 9.1(a) and 9.1(c) of the Agreement on Agriculture, in excess of the quantity commitment levels specified in Section II, Part IV of its Schedule.

6. The interpretation and correction of the European Communities' Schedule in light of the Modalities Paper

(a) Arguments of the parties

The European Communities considers that the Modalities Paper is an agreement reached by all participants in the Uruguay Round in connection with the conclusion of the Agreement on Agriculture. As such, the Modalities Paper is relevant as "context" for the interpretation of the schedules of reduction commitments, in accordance with Article 31.2 (a) of the Vienna Convention.

For the European Communities, the letter of the Chairman of the Market Access negotiating group of 20 December 1993 recorded the understanding of the Participants "that these negotiating modalities shall not be used as a basis for dispute settlement proceedings under the WTO Agreement". This means that the WTO Members cannot bring claims under the DSU based on the violation of the Modalities Paper. It does not mean, however, that the Modalities Paper is irrelevant for the interpretation of the Agreement on Agriculture. This is, as mentioned above, a question to be decided by the Panel having regard to the relevant provisions of the Vienna Convention.

For the European Communities, the fact that the Modalities Paper is not "legally binding" does not prevent it from being an "agreement" or from being "context". Thus, Article 31.2 of the Vienna Convention includes among the "context", the "preamble" of a treaty which, by definition, imposes no legal obligations. The European Communities adds that in any event, the Modalities Paper was drafted in mandatory terms and purported to be binding. Thus, Article 1 of the Modalities Paper states that:

"Specific binding commitments in the areas of market access, domestic support and export competition shall be established in accordance with the modalities set out hereunder."

The European Communities submits that the "base quantity" included in the EC Schedule is part of the text of the WTO Agreement. The European Communities asserts that total exports of sugar during the most recent marketing year for which there is data available (October 2001-September 2002) were 2,443,600 tonnes, i.e. 71,100 tonnes below the final commitment level as re-calculated in paragraph 4.124 above. Thus, the breach of the European Communities' reduction commitments alleged by the Complainants would result exclusively from a scheduling error.

Therefore, the European Communities submits that:

"[S]hould the Panel find that the C sugar regime provides export subsidies in excess of the reduction commitments, the only course of action consistent with the requirements of good faith would be for the Complainants to agree to the correction

654 See also paras. 4.122 et seq. above.
655 Including exports of C sugar, and adjusted for ACP/India sugar which is subject to a 1.6 million tonnes ceiling (see Section IV).
of the European Communities' scheduling commitments so as to include the exports of C sugar in the base levels and to rectify the annual commitments accordingly.\textsuperscript{656}

7.346 For the Complainants, the Modalities Paper does not provide "context" as defined in Article 31.2 of the Vienna Convention as it does not constitute an agreement relating to the Agreement on Agriculture made in connection with the conclusion of that Agreement. Instead, it constitutes merely an informal note issued by the Chairman of the Market Access Group on his own responsibility to assist the participants in the preparation of specific binding commitments included in the Schedules associated with the Agreement on Agriculture. In relation to Article 31.2(b) of the Vienna Convention, the Modalities Paper does not constitute an instrument relating to the Agreement on Agriculture made in connection with the conclusion of the Agreement. It does not represent an instrument made by one or more parties and, critically, it was a document prepared during the latter stages of negotiation of the Agreement, not at the time of its conclusion. While not providing "context" as defined in Article 31.2 of the Vienna Convention, the Modalities Paper does form part of the preparatory work, as recognised in Article 32 of the Vienna Convention, of the Agreement on Agriculture, having been developed as part of the negotiating process.

7.347 For the Complainants, the European Communities' arguments that its failure to include C sugar in its calculation of its base levels constitutes an error that it should be allowed to correct, has no foundation in the WTO Agreements or in WTO jurisprudence. Moreover, they consider that under the DSU, the Panel does not have the authority to permit the European Communities to "correct" its Schedule.\textsuperscript{657} Furthermore, they contend that the "error" of the European Communities is not "excusable" because "the decision on how to schedule support was one for each Member to take at the end of the day, based on its own interpretation of the application of the draft provisions to the regimes applying in each sector. Any risk in regard to so-called 'under-calculations' of the base period outlays and quantities was the responsibility of the scheduling Member, in this case the EC."\textsuperscript{658}

(b) Assessment by the Panel

7.348 The Panel recalls first that participants in the Uruguay Round submitted draft schedules essentially on the basis of the 1991 Draft Final Act Modalities. It also notes that the Modalities Paper was first issued in 1991 and then revised in December 1993 whereas discussions, among others on the scope of the Footnote inserted in the EC Schedule, went on thereafter and even after the European Communities submitted its final Schedule in March 1994. The version of the Modalities Paper (MTN.GNG/MA/W/24) referred to by the parties was prepared after the 15 December 1993 conclusion of the negotiation for the purpose of verification.

7.349 The Panel further recalls that the Modalities Paper cannot be the basis for dispute settlement under the WTO Agreement. The Panel also recalls that in EC – Bananas III the European Communities emphasized that: "[t]here was no doubt that any guidelines that existed for scheduling in the agricultural sector were left out of the Agreement on Agriculture on purpose".\textsuperscript{659} The Appellate Body also stated that "We note further that the Agreement on Agriculture makes no reference to the Modalities document ..."\textsuperscript{660}

\begin{footnotes}
\footnote{656} European Communities' first written submission, para. 142.
\footnote{657} Brazil's second written submission, para. 4 and Australia's second written submission, paras. 126-131.
\footnote{658} Australia's second written submission, para. 132.
\footnote{659} Panel Report on EC – Bananas III, para. 4.99.
\footnote{660} (footnote original) Modalities for the Establishment of Specific Binding Commitments Under the Reform Programme, MTN.GNG/MA/W/24, 20 December 1993.
\end{footnotes}
7.350 Clearly, the so-called Modalities Paper is not a covered agreement and thus cannot provide for WTO rights and obligations to Members. Nonetheless, it could be relevant when interpreting the Agreement on Agriculture, including Members' Schedules.

7.351 The Panel is of the view, that even if, arguendo, the Modalities Paper is to be considered as "context", within the meaning of Article 31.2 of the Vienna Convention and even if it becomes clear that the European Communities did not take account of its subsidies to C sugar in the calculation of its base quantity for export subsidies, this does not necessarily imply that the European Communities is now entitled to recalculate its base quantity.

7.352 Even if there were clear evidence that if the European Communities had known that C sugar was subsidized, it would have increased its base quantity to include additional subsidies to C sugar, the fact that the European Communities did not do so at the time, does not in and of itself entitle the European Communities to claim a correction of its Schedule today. WTO Members were not obliged to maintain export subsidies, they were only authorized to maintain them as exceptions to the prohibition in Articles 8 and 3.3 of the Agreement on Agriculture. Even if the interpretation provided by the Appellate Body in Canada – Dairy was novel as suggested by the European Communities, the fact remains that this Panel is bound by the wording of the WTO treaty and it does not have the competence to assess whether the European Communities at the time misinterpreted the scope of its obligations.

7.353 In the Panel's view, the European Communities' assertion that in light of the circumstances, the only course of action is for the Complainants to agree to the correction or revision of the European Communities' Schedule is not a matter for which the Panel has any authority as it goes beyond the scope of a panel recommendation which, according to Article 19.1 of the DSU, should be limited to recommending that the concerned Member "bring the measure into conformity with the Agreement on Agriculture". The Panel is not authorized, under the DSU, to force the Complainants to agree to such a correction or revision of the European Communities' Schedule.

7.354 Therefore, the only recommendation that this Panel can make, is for the European Communities to bring its measures into conformity with the Agreement on Agriculture. In the Panel's view this matter is of a multilateral nature and should not be resolved in the context of dispute settlement. The Panel notes that Members are free to negotiate and agree on a revision to the European Communities' Schedule or to agree on a waiver in that regard.

F. ARTICLE 10.1 OF THE AGREEMENT ON AGRICULTURE

1. Arguments of the parties

7.355 The Complainants submitted that should the Panel decide that the exports of C sugar were not subsidized by payments financed by virtue of governmental action within the meaning of Article 9.1(c) of the Agreement on Agriculture, the Panel should, in the alternative, address their claims under Article 10.1 of the Agreement on Agriculture.

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661 On the contrary the Appellate Body's interpretation of Article 9.1(c) would not seem to be a novel legal development but a confirmation or clarification of said provision.

662 Article 19.1 of the DSU provides: "Where a panel or the Appellate Body concludes that a measure is inconsistent with a covered agreement, it shall recommend that the Member concerned bring the measure into conformity with that agreement. In addition to its recommendations, the panel or Appellate Body may suggest ways in which the Member concerned could implement the recommendations."

663 See Section IV:D.2 above.
2. Assessment by the Panel

7.356 Since the Panel has found that the European Communities is acting inconsistently with Articles 3 and 8 of the Agreement on Agriculture, in providing producers/exporters of C sugar and ACP/India equivalent sugar, with payments on exports financed by virtue of the EC sugar regime, within the meaning of Article 9.1(a) and (c) of the Agreement on Agriculture in excess of the European Communities' commitment level, those subsidies cannot, by definition, be "export subsidies not listed in paragraph 1 of Article 9", as required by Article 10.1 of the Agreement on Agriculture.664

In this respect the Panel refers to the finding of the Appellate Body in Canada – Dairy (Article 21.5 – New Zealand and US) which held:

"It is clear from the opening clause of Article 10.1 that this provision is residual in character to Article 9.1 of the Agreement on Agriculture. If a measure is an export subsidy listed in Article 9.1, it cannot simultaneously be an export subsidy under Article 10.1."665

7.357 The Panel therefore sees no reason to examine the Complainant's claims under Article 10.1 of the Agreement on Agriculture.

G. NULLIFICATION OR IMPAIRMENT

1. Arguments of the parties

7.358 The Panel recalls that the parties' arguments are summarized in paragraphs 4.267-4.284 above.

7.359 Subsidiarily, the European Communities also submitted that even if the export of C sugar and the ACP/India sugar Footnote resulted in a violation of Articles 3.3, 8 or 10.1 of the Agreement on Agriculture, such violation would not nullify or impair any benefits accruing to the complaining parties.

7.360 The European Communities submitted that Article 3.8 of the DSU made clear that, while a finding of violation of a covered agreement gave rise to a presumption of nullification or impairment of benefits accruing under that agreement, the defending party had an opportunity to rebut such presumption. In the opinion of the European Communities, the ordinary meaning of the term "adverse impact" in Article 3.8 of the DSU did not require that the defending party had to show that the alleged violation had had no actual effect on the Complainants' exports to establish the absence of such impact. The European Communities submitted that it had shown that the Complainants had suffered no "adverse impact" because they could not have expected that the European Communities would stop exporting C sugar.

7.361 The European Communities argued that if it were to reduce its exports of sugar by 60 per cent, as requested by the Complainants, it would be doing much more than removing any "adverse impact". The European Communities submitted that, if nevertheless the Panel were of the view that the Complainants were entitled to expect that the European Communities would reduce its exports of C sugar and ACP/India equivalent sugar, such expectations would be limited to a 21 per cent reduction, as envisaged in the Modalities Paper with respect to all export subsidies, rather than their complete elimination. Accordingly, the alleged violation of Articles 3, 8 and 10.1 of the Agreement on Agriculture would nullify or impair benefits accruing to the Complainants only to the

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extent that the current volume of subsidized exports exceeded 79 per cent of the quantity of subsidized exports made during the base period.

7.362 The Complainants considered that the EC's infringement of its obligations under the *Agreement on Agriculture* had resulted in a prima facie case that nullification and impairment had been suffered by the Complainants. They agreed with the European Communities that, pursuant to Article 3.8 of the *DSU*, the European Communities, as the defending party, could rebut the presumption of nullification and impairment but submitted that in doing so, it must, under Article 3.8 of the *DSU*, establish that its breach of the rules had not had "an adverse impact" on the complainant(s).

7.363 Furthermore, the Complainants provided evidence that the EC sugar regime caused them losses. The Complainants referred to a March 2004 Oxfam study which had calculated, based on 2002 exports, that the EC sugar regime caused immediate losses of $494 million for Brazil and $151 million for Thailand in that year alone. Brazil submitted that that was serious nullification or impairment by any reasonable standard. The Complainants also referred to this report which noted the cost of the EC sugar regime to South Africa and a number of other developing countries, and recalled that the Panel had heard directly from Colombia and Paraguay, as third parties, that such regime hurt them as well.

7.364 The European Communities responded that the Complainants' arguments overlooked the thrust of the European Communities' defence, which was precisely that the Complainants could have no "legitimate expectations" that the European Communities would stop its exports of C sugar. At most, the Complainants could have expected that the European Communities would reduce those exports by 21 per cent (in quantity) as agreed in the Modalities Paper.

7.365 All parties agreed that the nullification or impairment allegedly suffered as a result of the WTO inconsistencies of the EC sugar regime would not differ based on the particular agreement violated. The Complainants clarified, however, that if the elements of a violation under the *Agreement on Agriculture* and the *SCM Agreement* are established, then they are entitled to the remedies for nullification or impairment established by each agreement, provided there is no overlap or duplication in any remedies actually imposed.

2. **Assessment by the Panel**

7.366 The Panel recalls the text of Article 3.8 of the *DSU* which provides that the prima facie presumption of nullification and impairment may be rebutted:

"In cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered *prima facie* to constitute a case of nullification or impairment. This means that there is normally a presumption that a breach of the rules has an adverse impact on other Members parties to that covered agreement, and in such cases, *it shall be up to the Member against whom the complaint has been brought to rebut the charge.*" (emphasis added)

7.367 The Panel further recalls that in *EC – Bananas III*, the Appellate Body observed that the European Communities, in its appeal, attempted to "rebut the presumption of nullification or

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666 Exhibit ALA -12, pages 2 and 28.
667 Brazil's closing statement at the second substantive meeting of the Panel, para. 2, Colombia's oral statement, para. 2 and Paraguay's oral statement, para. 2.
668 Parties' replies to Panel question No. 2.
impairment on the basis that the United States has never exported a single banana to the European Community, and therefore, could not possibly suffer any trade damage.” The Appellate Body stated:

"[W]e note that the two issues of nullification or impairment and of the standing of the United States are closely related….[T]wo points are made that the Panel may well have had in mind in reaching its conclusions on nullification or impairment. One is that the United States is a producer of bananas and that a potential export interest by the United States cannot be excluded; the other is that the internal market of the United States for bananas could be affected by the EC bananas regime and by its effects on world supplies and world prices of bananas….They are…relevant to the question whether the European Communities has rebutted the presumption of nullification or impairment. (emphasis added)

So, too, is the panel report in United States—Superfund, to which the Panel referred. In that case, the panel examined whether measures with 'only an insignificant effect on the volume of exports do nullify or impair benefits under Article III:2 …'. The panel concluded (and in so doing, confirmed the views of previous panels) that:

'Article III:2, first sentence, cannot be interpreted to protect expectations on export volumes; it protects expectations on the competitive relationship between imported and domestic products. A change in the competitive relationship contrary to that provision must consequently be regarded ipso facto as a nullification or impairment of benefits accruing under the General Agreement. A demonstration that a measure inconsistent with Article III:2, first sentence, has no or insignificant effects would therefore in the view of the Panel not be a sufficient demonstration that the benefits accruing under that provision had not been nullified or impaired even if such a rebuttal were in principle permitted.\(^\text{669}\)

The panel in United States—Superfund subsequently decided 'not to examine the submissions of the parties on the trade effects of the tax differential' on the basis of the legal grounds it had enunciated. The reasoning in United States—Superfund applies equally in this case.\(^\text{670}\) (emphasis added)

7.368 The Panel also notes that in the panel on Turkey—Textiles, Turkey argued that even if its quantitative restrictions on imports of textile and clothing products from India were in violation of WTO law, India had not suffered any nullification or impairment of its WTO benefits within the meaning of Article 3.8 of the DSU because imports of textile and clothing from India had increased since the Turkish measures at issue had entered into force. The panel rejected this argument in a finding not reviewed by the Appellate Body:

"We are of the view that it is not possible to segregate the impact of the quantitative restrictions from the impact of other factors. While recognizing Turkey's efforts to liberalize its import regime on the occasion of the formation of its customs union with the European Communities, it appears to us that even if Turkey were to demonstrate that India's overall exports of clothing and textile products to Turkey have increased from their levels of previous years, this would not be sufficient to rebut the presumption of nullification and impairment caused by the existence of WTO incompatible import restrictions. Rather, at minimum, the question is whether

\(^\text{669}\) (footnote original) GATT Panel Report on US—Superfund, para. 5.1.9.

exports have been what they would otherwise have been, were there no WTO incompatible quantitative restrictions against imports from India. Consequently, we consider that even if the presumption in Article 3.8 of the DSU were rebuttable, Turkey has not provided us with sufficient information to set aside the presumption that the introduction of these import restrictions on 19 categories of textile and clothing products has nullified and impaired the benefits accruing to India under GATT/WTO.” 671 (emphasis added)

7.369 The European Communities cites the findings of the Appellate Body in India – Patents (US) to conclude that the existence of nullification or impairment should be assessed by looking at the legitimate expectations of the Complainants. The Panel recalls that in that case, the Appellate Body rejected the panel’s conclusion that the protection of “legitimate expectations” is used in GATT acquis as a principle of interpretation.672 In this context, the Appellate Body made clear that the “legitimate expectations of the parties to a treaty are reflected in the language of the treaty itself” and that this course of action should not include the “imputation into a treaty of words that are not there or the importation into a treaty of concepts that were not intended.”673 More importantly, in that dispute, the panel and the Appellate Body had resorted to reliance on expectations to establish a violation, whereas in this case, the European Communities’ argumentation refers to the nullification or impairment of benefits that may or may not result from an established violation.

7.370 In the Panel’s view, the European Communities’ reliance on the Complainants’ general expectations or lack thereof, is not sufficient to rebut the presumption of nullification of benefits pursuant to Article 3.8 of the DSU, once a violation has been demonstrated.674 The Complainants, as with all Members, had legitimate expectations that the competitive relationship of their sugar would not be nullified or impaired by the export subsidies of the European Communities provided in excess of the European Communities’ commitment level. The Complainants also had legitimate expectations that the European Communities would comply with the Agreement on Agriculture, including the European Communities’ obligation not to provide export subsidies above its commitment level.

7.371 The Panel recalls that the flexibilities provided for by Article 9.2(b)(iv) of the Agreement on Agriculture is an exception to the general prohibition against export subsidies provided for in Article 8 and 3.3 of the Agreement on Agriculture. Therefore, the European Communities had the right, but was not obliged, to maintain export subsidies if it had scheduled them and if it respected its reduction commitment pursuant to Article 9.2(b)(iv) of the Agreement on Agriculture. The Complainants were entitled to expect that the European Communities put an end to or reduce its export subsidies in place prior to the Uruguay Round.

671 Panel Report on Turkey – Textiles, para. 9.204.
672 Appellate Body Report on India – Patents (US), paras. 39-42. The Appellate Body had considered in that instance that the panel had confused two different concepts from previous GATT practice: (i) the protection of expectations of contracting parties as to the competitive relationship between their products and the products of other contracting parties (in the context of violation complaints under Articles III and XI of the GATT); and (ii) the protection of the reasonable expectations of contracting parties relating to market access concessions (in the framework of non-violation complaints under Article XXIII:1(b) of the GATT).
673 Appellate Body Report on India – Patents (US), paras. 43-45.
674 European Communities’ first written submission, para. 147.
675 The Panel recalls that Article 3.8 of the DSU is a codification of GATT practice providing for the same presumption. The Panel also recalls that such a presumption has never been rebutted, except in the exceptional panel report on US – Section 301 Trade Act. The panel in US – Section 301 Trade Act recognized that the United States had rebutted a prima facie presumption because it found that the United States had already lawfully removed the prima facie violation of Section 304. In that instance, the US Executive Office had made a “mandatory” promise to render determinations under Section 304 in conformity with its WTO obligations (in the SAA). This for the panel override the prima facie case of violation found earlier on. See Panel Report on US – Section 301 Trade Act, paras. 7.109-7.113.
Moreover, the Panel notes that the European Communities has not rebutted the evidence submitted by the Complainants with regard to the amount of trade lost by the Complainants as a result of the EC sugar regime. The Panel recalls that "a prima facie case is one which, in the absence of effective refutation by the defending party, requires a panel, as a matter of law, to rule in favour of the complaining party presenting the prima facie case".\footnote{Appellate Body Report on EC – Hormones, para. 104.}

The Panel is, therefore, of the view that the European Communities has not effectively refuted the Complainants' allegation that the European Communities' violations nullified or impaired the benefits to which they are entitled. In particular, the European Communities has not submitted sufficient factual evidence to suggest that the Complainants did not suffer an "adverse impact" from the European Communities' exports of C sugar and ACP/India equivalent sugar provided in excess of the European Communities' commitment level. The fact that the Complainants did not bring their claims forward earlier does not relieve the European Communities from adducing sufficient arguments and evidence to rebut the presumption in Article 3.8 of the DSU.

Consequently, the Panel finds that the European Communities' violations of the Agreement on Agriculture nullified or impaired the benefits to which the Complainants were entitled under the Agreement on Agriculture.

H. ARTICLE 3 OF THE SCM AGREEMENT

1. Arguments of the parties

The arguments of the parties are summarized in paragraphs 4.232 to 4.266 of this Panel report.

The Complainants submit that the export subsidies granted in respect of exports of quota sugar, ACP/India equivalent sugar and C sugar were prohibited subsidies under the SCM Agreement. More specifically, the Complainants claimed that the EC sugar regime provided subsidies that amounted to an export subsidy listed in Item (d) of the Illustrative List of Export Subsidies in Annex I of the SCM Agreement (hereinafter the "Illustrative List of the SCM Agreement") and that the export refund on exports of ACP/India "equivalent" sugar amounted to an export subsidy listed in Item (a) of the same Illustrative List. Furthermore, Australia and Brazil claimed that the EC sugar regime was also otherwise inconsistent with Article 3.2 of the SCM Agreement.

The European Communities argued that the SCM Agreement was not applicable to agricultural products. It pointed to, inter alia, Article 21.1 of the Agreement on Agriculture and claimed that this provision had been interpreted by the Appellate Body as meaning that the other Annex IA Agreements applied "except to the extent that the Agreement on Agriculture contains specific provisions dealing specifically with the same matter."\footnote{Appellate Body Report on EC – Bananas III, para. 155.} The European Communities contended that it was clear that the Agreement on Agriculture contained specific provisions dealing specifically with the "same matter".\footnote{For the European Communities, this would nevertheless not render Article 13(c) meaningless because Article 13 in general, and Article 13(c) in particular, were intended to provide added clarity to the relationship between the two agreements during a specific time-period (the nine year implementation period for Article 13).} For the European Communities, applying the SCM Agreement to agricultural export subsidies (even those granted inconsistently with the Agreement on Agriculture), and specifically the prohibition on export subsidies, would undermine the specificity of the agricultural regime, and the gradual process of reform which all Members signed up to.
7.378 The Complainants reiterated that there were essentially three differences between the remedy, and the implementation of recommendations and rulings, provided by Articles 19 to 21 of the DSU and that provided by Article 4.7 of the SCM Agreement pertaining to the nature of the remedy, the time-frame and the procedural aspects. Of these differences the last was of particular importance to the Complainants in order to avoid further negotiations with the European Communities and possibly a lengthy and complex arbitration procedure to resolve a matter that could and should be resolved by this Panel.

7.379 The European Communities responded that the application of Article 4.7 of the SCM Agreement would amount to nullifying the rights of WTO Members under the Agreement on Agriculture.

2. Assessment by the Panel

7.380 The Panel recalls that, in this dispute, it has followed the order of examination advanced by the Appellate Body in Canada – Dairy (Article 21.5 New Zealand and US) in relation to the Agreement on Agriculture and the SCM Agreement, where the Appellate Body stated that Article 3.1 of the SCM Agreement "indicates that the WTO-consistency of an alleged export subsidy for agricultural products has to be examined, in the first place, under the Agreement on Agriculture." This approach was supported by all parties to the present dispute.

7.381 The Panel has already found the EC sugar regime to be inconsistent with the European Communities' export subsidy obligations under both Article 3.3 and Article 8 (through Article 9.1(a) and Article 9.1(c)) of the Agreement on Agriculture. In principle, therefore, the Panel could also examine the Complainants claims that the regime, or parts thereof, constitute an export subsidy inconsistent with Article 3 of the SCM Agreement, in accordance with the Panel's terms of reference. The question that arises is whether the Panel should examine these claims, or whether it should rather apply the principle of judicial economy.

7.382 The Panel recalls that the Appellate Body in Australia – Salmon, referred to earlier by the parties, clarified when judicial economy can be exercised and cautioned against a panel providing only a partial resolution of the matter at issue:

"The principle of judicial economy has to be applied keeping in mind the aim of the dispute settlement system. This aim is to resolve the matter at issue and 'to secure a positive solution to a dispute'. To provide only a partial resolution of the matter at issue would be false judicial economy. A panel has to address those claims on which a finding is necessary in order to enable the DSB to make sufficiently precise recommendations and rulings so as to allow for prompt compliance by a Member with those recommendations and rulings 'in order to ensure effective resolution of disputes to the benefit of all Members'.” (emphasis added).

Although the Australia – Salmon dispute did not involve a claim under the SCM Agreement, we believe that the principles it sets forth regarding the exercise of judicial economy are relevant to WTO dispute settlement generally.

7.383 The Complainants claim that the Panel is entitled to examine the Complainants' export subsidy claims under Article 3 of the SCM Agreement because the EC sugar regime is inconsistent

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680 See for example Brazil's second written submission para. 75.
with the European Communities' export subsidy commitments under the Agreement on Agriculture.\(^{682}\)

As a matter of logic, therefore, it would appear that the European Communities would, by fully implementing a recommendation by the DSB to bring the European Communities' sugar regime into conformity with its obligations under the Agreement on Agriculture, also preclude any finding in the context of a review procedure under Article 21.5 of the DSU that the regime is inconsistent with the export subsidy disciplines of the SCM Agreement. Accordingly, the Panel's findings under the Agreement on Agriculture should be sufficient to fully resolve the matter at issue.

7.384 The Complainants appear to be of the view that the Panel must examine their export subsidy claims under Article 3 of the SCM Agreement so that they may obtain the benefits of a recommendation under Article 4.7 of that Agreement that the European Communities withdraw the subsidy "without delay" and the specification of the time period within which the measure must be withdrawn. They emphasize in this respect the reference by the Appellate Body in Australia – Salmon to the need to make such findings as are necessary to ensure prompt compliance. There is some issue as to whether this Panel is entitled to make such a recommendation and to specify such a time period in the circumstances before it.\(^{683}\) In any event, it seems to the Panel that the Appellate Body's concern in Australia – Salmon was to ensure that a panel's findings be sufficiently complete so as to inform the Member as to what needs to be done, rather than on when it needs to be done. The Panel doubts that the Appellate Body considered that the application of the normal rules regarding the timing of implementation, applicable in most WTO disputes, would not constitute prompt compliance, and it does not believe that the Appellate Body's reasoning requires it to decide claims not necessary to the full resolution of the matter before the Panel merely in order to obtain what might – but would not necessarily be – more rapid compliance.

7.385 Referring to Article 19.2 of the DSU, Australia contends that a decision to exercise judicial economy in respect of the Complainants' SCM Agreement claims would diminish its rights under a covered agreement in regard to the implementation time period in the event of its claims succeeding. The Panel notes that, under Article 4.7 of the SCM Agreement, a panel shall make its recommendation, including the time period for implementing this recommendation, "[i]f the measure in question is found to be a prohibited subsidy". Similarly, Article 19.1 of the DSU provides that a panel shall make its recommendation "[w]here a panel or the Appellate Body concludes that a measure is inconsistent with a covered agreement". While these provisions govern the obligations of panels where they make findings of inconsistency, they do not, in the Panel's opinion, prevent panels from exercising judicial economy in the appropriate circumstances. Thus, the Panel does not agree that its decision to exercise judicial economy in the present case diminishes Australia's rights within the meaning of Article 19.2 of the DSU.

7.386 Finally, the Panel notes that the Complainants' have not set forth their claims under Article 3 of the SCM Agreement in quite as clear and unambiguous a manner as under the Agreement on Agriculture. Rather, the Complainants have focused on their claims under the Agreement on Agriculture. Panels depend upon the active participation of the parties to clarify and develop the issues presented in a dispute. The Panel considers that the important questions presented under the SCM Agreement in this dispute would be best decided in a case where they have been further argued by the parties. In this connection, the Panel especially notes that many of the Complainants' references to the SCM Agreement were made in the context of their claims under the Agreement on Agriculture.

\(^{682}\) Brazil's second written submission, title F and paras. 75 and 76; Thailand's first written submission para. 113 and Australia's first written submission, paras. 189-193 and second written submission, paras. 67-71 and 100-101.

For these reasons, the Panel exercises judicial economy and declines to examine the Complainants' export subsidy claims under Article 3 the SCM Agreement.

VIII. CONCLUSIONS, RECOMMENDATION AND SUGGESTION

A. CONCLUSIONS

8.1 The Panel concludes that:

(a) the European Communities’ budgetary outlay and quantity commitment levels for exports of subsidized sugar is determined with reference to the entry specified in Section II, Part IV of its Schedule and the content of Footnote 1 in relation to these entries is of no legal effect and does not enlarge or otherwise modify the European Communities' specified commitment levels.

(b) the European Communities’ quantity commitment level for exports of sugar pursuant to Articles 3.3, and 8 of the Agreement on Agriculture is 1,273,500 tonnes per year, with effect from the marketing year 2000/2001.

(c) the European Communities’ budgetary outlay commitment level for exports of sugar pursuant to Articles 3.3, and 8 of the Agreement on Agriculture is €499.1 million per year, with effect from the marketing year 2000/2001.

(d) the Complainants have provided prima facie evidence that since 1995 the European Communities' total exports of sugar exceed its quantity commitment level. In particular, in the marketing year 2000/2001 the European Communities' exported 4,097,000 tonnes of sugar, i.e. 2,823,500 tonnes in excess of its commitment level.

(e) there is prima facie evidence that the European Communities has been providing export subsidies within the meaning of Article 9.1(a) of the Agreement on Agriculture to what it considers to be exports of "ACP/India equivalent sugar" since 1995.

(f) there is prima facie evidence that the European Communities has been providing export subsidies within the meaning of Article 9.1(c) of the Agreement on Agriculture to its exports of C sugar since 1995.

8.2 In light of Article 10.3 of the Agreement on Agriculture, the Panel concludes that the European Communities has not demonstrated that its exports of sugar in excess of its commitment level are not subsidized.

8.3 Therefore, the Panel concludes that the European Communities, through its sugar regime, has acted inconsistently with its obligations under Articles 3.3 and 8 of the Agreement on Agriculture, by providing export subsidies within the meaning of Article 9.1(a) and (c) of the Agreement on Agriculture in excess of (i) its quantity commitment level specified in Section II, Part IV of its Schedule, which since the marketing year 2000/2001 is for 1,273,500 tonnes of sugar and (ii) its budgetary outlay commitment level specified in Section II, Part IV of its Schedule, which since the marketing year 2000/2001 is €499.1 million per year.

8.4 Since Article 3.8 of the DSU provides that "[i]n cases where there is an infringement of the obligations assumed under a covered agreement, the action is considered prima facie to constitute a case of nullification or impairment", the Panel concludes that – to the extent the European Communities has acted inconsistently with its obligations under the Agreement on Agriculture – it has nullified or impaired benefits accruing to Australia under the Agreement on Agriculture.
B. RECOMMENDATION

8.5 In light of the above conclusions, the Panel recommends that the Dispute Settlement Body request the European Communities to bring its EC Council Regulation No. 1260/2001, as well as all other measures implementing or related to the European Communities' sugar regime, into conformity with its obligations in respect of export subsidies under the Agreement on Agriculture.

C. SUGGESTION BY THE PANEL

8.6 The Panel is aware of the concerns and interests expressed, in the context of these proceedings, by several developing countries, with regard to their continued preferential access to the EC market for their sugar exports.

8.7 Pursuant to Article 19.1 of the DSU, the Panel suggests that in bringing its exports of sugar into conformity with its obligations under Articles 3.3 and 8 of the Agreement on Agriculture, the European Communities consider measures to bring its production of sugar more into line with domestic consumption whilst fully respecting its international commitments with respect to imports, including its commitments to developing countries.

8.8 In this regard, the Panel notes the recent statement of the European Communities on 14 July 2004 that the European Communities "fully stands by its commitments to ACP countries and India" and that with the reform of its sugar regime, the ACP countries and India will "get a clear perspective, keep their import preferences and retain an attractive export market."

**ANNEX A**

**LIST OF EXHIBITS SUBMITTED BY THE PARTIES**

<table>
<thead>
<tr>
<th>EXHIBIT</th>
<th>CONFIDENTIAL (C)</th>
<th>FULL TITLE</th>
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</thead>
<tbody>
<tr>
<td>ALA-2</td>
<td></td>
<td>GATT, AG/W/9, 26 June 1984, Special distribution, Committee on Trade in Agriculture, Draft Recommendations – Explanatory note by the Secretariat</td>
</tr>
<tr>
<td>ALA-3</td>
<td></td>
<td>G8, Technical Discussions on Agriculture Schedules, Geneva, 23 to 26 March 1992 - Record of Discussion</td>
</tr>
<tr>
<td>ALA-4</td>
<td></td>
<td>Letter from Trần Van-Thinh, EC Permanent Representative, to Arthur Dunkel, Director-General, GATT, Chairman of the TNC, 4 March 1992 – agricultural negotiations – Draft commitments (schedules)</td>
</tr>
<tr>
<td>ALA-5</td>
<td></td>
<td>Uruguay Round – Agriculture, 10 December 1993 letter and accompanying paper, Issues Requiring Settlement – Australia, from Australian Minister for Trade, Peter Cook, to Mr Steichen EU Commissioner for Agriculture &amp; Rural Development</td>
</tr>
<tr>
<td>ALA-6</td>
<td></td>
<td>14 December 1993 Letter from Trần Van-Thinh EC Permanent Representative, to Peter Sutherland, Director-General GATT - agricultural negotiations – draft commitments (schedules)</td>
</tr>
<tr>
<td>ALA-7</td>
<td></td>
<td>25 March 1994 Letter from Hervé Jouanjean, Deputy Head of EC Delegation, to A. Hoda, Deputy Director-General GATT – agricultural negotiations – draft commitments (schedules)</td>
</tr>
<tr>
<td>ALA-9</td>
<td></td>
<td>Judgment of the Court (Sixth Chamber) - 10 January 2002(1), (Agriculture – Common organisation of the markets – Sugar – Attribution as C sugar of a quantity of sugar produced during a given marketing year – Charge payable in respect of sugar disposed of on the international market – Levied in the case of export with an export licence – Export refunds) Case C-101/99.</td>
</tr>
<tr>
<td>ALA-10</td>
<td></td>
<td>Opinion of Advocate General Stix-Hackl delivered on 10 September 2003(1) Case C-329/01 The Queen on the application of British Sugar plc v Intervention Board for Agriculture Produce, (Reference for a preliminary ruling from the High Court of Justice of England &amp; Wales, Queen's Bench Division (Administrative Court)) (Common organisation of the markets in the sugar sector – Export licence for C sugar – Proof of export – Correction of licence – Principle of proportionality – Penalty)</td>
</tr>
<tr>
<td>ALA-12</td>
<td></td>
<td>Oxfam Briefing Paper 61, <em>Dumping on the world - How EU sugar policies hurt poor countries</em>, March 2004</td>
</tr>
</tbody>
</table>
BRA-1 C Considerations over C Sugar Production and Exports in the European Communities, report prepared by Plinio M. Nastari, Ph.D., Datagro, Brazil

BRA-2 C LMC Data

COMP-1 European Communities Court of Auditors, *Special Report No 20/2000 (pursuant to Article 248, paragraph 4 (2), EC) concerning the management of the Common Organisation of the Market for Sugar* together with the Commission's replies 2000

COMP-2 Netherlands Economic Institute, *Evaluation of the Common Organisation of the Markets in the Sugar Sector* (prepared for the Commission of the European Communities), September 2000

COMP-3 Oxfam Briefing Paper 27, *The Great EU Sugar Scam, How Europe's sugar regime is devastating livelihoods in the developing world*, August 2002


COMP-5 EC Regulations


C. Commission Regulation (EC) No 1440/2002 of 7 August 2002 revising the maximum amount for the B production levy and amending the minimum price for B beet in the sugar sector for the 2002/03 marketing year


G. Commission Regulation (EC) 1520/2000 of 13 July 2000, laying down common detailed rules for the application of the system of granting export refunds on certain agricultural products exported in the form of goods not covered by Annex I to the Treaty, and the criteria for fixing the amount of such refunds

H. Council Regulation (EC) No 2201/96 of 28 October 1996 on the common organization of the markets in processed fruit and vegetable products

I. Commission Regulation (EC) No 2315/95 of 29 September 1995 laying down detailed rules for the application of export refunds to certain sugars covered by the common organization of the market in sugar used in certain products processed from fruit and vegetables

K. Council Regulation (EC) No 3448/93 of 6 December 1993 laying down the trade arrangements applicable to certain goods resulting from the processing of agricultural products

L. Commission Regulation (EEC) No 65/82 of 13 January 1982 laying down detailed rules for carrying forward sugar to the following marketing year.


COMP-7 Commission of the European Communities, Sugar: International Analysis Production Structures within the EU, 22 September 2003

COMP-8 Commission of the European Communities, Common Organisation of the Sugar Market, Description [europa.eu.int/comm/agriculture/markets/sugar/index_en.htm]

COMP-9 European Communities Court of Auditors, Extracts from Annual Report concerning the financial year 2001 2002/C 295/01, 28 November 2002

COMP-10 Commission of the European Communities, Official Journal L103/1, 24.4.2003, Commission Decision of 20 December 2001 declaring a concentration to be compatible with the common market and the EEA Agreement, (Case COMP/M.2530 - Südzucker/Saint Louis Sucre), (C(2001) 4524)

COMP-11 European Communities Court of Auditors, Special Report No 9/2003 (pursuant to article 248, (4), second subparagraph, EC) concerning the system for setting the rates of subsidy on exports of agricultural products (Export Refunds) together with the Commission's replies, 2003/C 211/01, 5 September 2003

COMP-12 Commission of the European Communities - Commission Responds to Court of Auditors' report on the sugar market organization, press release BIO/00/214, 9 November 2000

COMP-13 Commission of the European Communities, Commission clears acquisition of Saint Louis Sucre by Südzucker subject to commitments, press release IP/01/1891, 20 December 2001

COMP-14 European Communities (EC, EURATOM), extracts from Preliminary Draft general budget of the European Communities for the financial year 2004 Volume 1, 13 June 2003


COMP-16 Schedule CXL: European Communities, Extract from Part I: Most-Favoured-Nation Tariff, Section I – Agricultural Products

Section I – B Tariff Quotas

Part IV – Agricultural Products: Commitments Limiting Subsidization, Article 3 of the Agreement on Agriculture)

Section II: Export Subsidies: Budgetary Outlay and Quantity Reduction Commitments
<table>
<thead>
<tr>
<th>EXHIBIT</th>
<th>CONFIDENTIAL (C)</th>
<th>FULL TITLE</th>
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<tr>
<td>COMP-17</td>
<td>WTO Committee on Agriculture, notifications concerning export subsidy commitments (Tables ES:1 to ES:3) received from the delegation of the European Communities for marketing years 1995/1996 to 2001/2002, G/AG/N/EEC/5, 11, 20, 23, 32, 36, 44.</td>
<td></td>
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<td>COMP-18</td>
<td>WTO Committee on Agriculture, notifications concerning domestic support commitments, (Table DS:1 and the relevant supporting tables) received from the delegation of the European Communities for marketing years 1995/1996 through to 1999/2000, G/AG/N/EEC/12, 16, 26, 30, 38</td>
<td></td>
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<tr>
<td>COMP-19</td>
<td>Negotiating Group on Market Access - 20 December 1993, Modalities for the Establishment of Specific Binding Commitments under the Reform Programme, Note by the Chairman of the Market Access Group, MTN.GNG/MA/W/24</td>
<td></td>
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<tr>
<td>COMP-20</td>
<td>Blair House Agreement, Exchanges of letters regarding the oilseeds agreement between EC Commission Vice-President With Special Responsibility For External Relations and Commercial Policy and the United States Trade Representative, 2 and 4 December 1992</td>
<td></td>
</tr>
<tr>
<td>COMP-22</td>
<td>WTO Ministerial Conference Fourth Session Doha, 9-14 November 2001, Summary Record of the Ninth Meeting WT/MIN(01)/SR/9, 10 January 2002</td>
<td></td>
</tr>
<tr>
<td>EC-1</td>
<td>Export subsidy commitments in Schedule CXL – EC</td>
<td></td>
</tr>
<tr>
<td>EC-2</td>
<td>Draft Final Act Embodying the Results of the Uruguay Round of Multilateral Trade Negotiations, MTN.TNC/W/FA, 20 December 1991, Section L (&quot;Text on Agriculture&quot;), Part B (&quot;Agreement on Modalities for the Establishment of Specific Binding Commitments under the Reform Program2</td>
<td></td>
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<td>EC-3</td>
<td>Modalities for the Establishment of Specific Binding Commitments, MTN.GNG/MA/W/24, 20 December 1993</td>
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<td>EC-4</td>
<td>Draft schedule of commitments submitted on 16 December 1992</td>
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<tr>
<td>EC-5</td>
<td>Letter of 4 March 1992 and Supporting Table 11 attached to that letter</td>
<td></td>
</tr>
<tr>
<td>EC-6</td>
<td>Draft schedule of commitments submitted on 14 December 1993</td>
<td></td>
</tr>
<tr>
<td>EC-7</td>
<td>List of bilateral meetings between the EC and other participants</td>
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</tr>
<tr>
<td>EC-8</td>
<td>EC Commission minutes of the meeting with Australia of 3 December 1993</td>
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<td>EC-9</td>
<td>Export subsidy commitments in Schedule LXXX- EC</td>
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<tr>
<td>EC-10</td>
<td>Minutes of the DSB meeting of 18 December 2001, WT/DSB/M/116</td>
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<td>EC-11</td>
<td>Minutes of the DSB Meeting of 17 January 2003, WT/DSB/M/141</td>
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<td>EC-12</td>
<td>Uruguay Round Outcomes – Agriculture, July 1994, Agriculture Branch, Trade Negotiations and Organisations Divisions, Department of Foreign Affairs and Trade, Canberra, Australia</td>
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<td>EC-13</td>
<td>Uruguay Round Outcomes – Agriculture provided the basis for the document Implications of the GATT Uruguay Round for the Sugar Industry, An Australian Perspective, ABARE Conference Paper 94.19</td>
<td></td>
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<td>EC-14</td>
<td>International Policies Affecting Market Expansion, ABARE, 1999</td>
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<td>EC-15</td>
<td></td>
<td><em>Effects of the Uruguay Round Agreement on U.S. Agricultural Commodities</em>, USDA, March 1994</td>
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<tr>
<td>EC-16</td>
<td></td>
<td><em>Sample control sheet for export refunds under the sugar CMO</em>, DG Agriculture, European Commission</td>
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<td>EC-17</td>
<td>C</td>
<td><em>Update of Sugar Policy in Selected Countries</em>, LMC International</td>
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<tr>
<td>EC-20</td>
<td></td>
<td>Excerpt from <em>Background Information on Selected Policy Issues in the Sugar Sector</em>, OECD, June 2002</td>
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<td>EC-22</td>
<td>C</td>
<td>Excerpts from the <em>LMC Worldwide Survey of Sugar and HFCS Production Costs</em>, 2003 Report</td>
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<tr>
<td>EC-23</td>
<td>C</td>
<td>Profitability of the export sales of the major sugar exporters, according to LMC data</td>
</tr>
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<td>EC-24</td>
<td></td>
<td>Letter dated 10 December 1993 from Mr Peter Cook, Australia’s Minister of Trade to Mr René Steichen, Commissioner for Agriculture of the European Commission</td>
</tr>
<tr>
<td>EC-25</td>
<td></td>
<td>Production, carry over and exports of C sugar by French producers</td>
</tr>
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<td>EC-26</td>
<td></td>
<td>Ministerial Communiqué of 23 February 1994</td>
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<td>EC-27</td>
<td></td>
<td>Section II, Part IV of Canada’s and New Zealand’s schedules of export subsidy commitments</td>
</tr>
</tbody>
</table>
## ANNEX B

**Scheduled export subsidy commitment levels (quantities), and notified total exports**

<table>
<thead>
<tr>
<th>Scheduled implementation period</th>
<th>Scheduled quantity levels</th>
<th>Commitment level alleged by the EC</th>
<th>Notified total exports</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Marketing year starting 1 October/30 September</strong></td>
<td>Thousand tonnes, white sugar equivalent</td>
<td>“Annual reduction commitments + 1.6 million tons ACP/India equivalent”</td>
<td>Thousand tonnes, product weight basis</td>
</tr>
<tr>
<td>1995/1996</td>
<td>1,555.6</td>
<td>3,155.6</td>
<td>4,544.4 (3)</td>
</tr>
<tr>
<td>1996/1997</td>
<td>1,499.2</td>
<td>3,099.2</td>
<td>4,536.0 (3)</td>
</tr>
<tr>
<td>1997/1998</td>
<td>1,442.7</td>
<td>3,042.7</td>
<td>5,670.4 (3)</td>
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<tr>
<td>1998/1999</td>
<td>1,386.3</td>
<td>2,986.3</td>
<td>5,116.3 (3)</td>
</tr>
<tr>
<td>1999/2000</td>
<td>1,329.9</td>
<td>2,929.9</td>
<td>5,669.0 (3)</td>
</tr>
<tr>
<td>2000/2001</td>
<td>1,273.5</td>
<td>2,873.5</td>
<td>6,023.0</td>
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<tr>
<td>2001/2002</td>
<td>1,273.5</td>
<td>2,873.5</td>
<td>4,097.0</td>
</tr>
</tbody>
</table>

1. Schedule CXL.
2. Table ES:2 notifications to the WTO Committee on Agriculture (G/AG/N/EEC/5/Rev.1; EEC/11; EEC/20/Rev.1; EEC/23; EEC/32; EEC/36; EEC/44).
3. Year starting 1 July to 30 June.

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685 See Table 11 of the European Communities' first written submission. The Panel presumes that the marketing years and the measurement units are identical to those specified in Schedule CXL.
**ANNEX C**

**SCHEDULE CXL – EUROPEAN COMMUNITIES**

This Schedule is authentic only in the English language.

**PART IV – AGRICULTURAL PRODUCTS: COMMITMENTS LIMITING SUBSIDIZATION**

(Article 3 of the Agreement on Agriculture)

**SECTION II: Export Subsidies: Budgetary Outlay and Quantity Reduction Commitments**

<table>
<thead>
<tr>
<th>Description of products and tariff item numbers at HS six digit level (*)</th>
<th>Base outlay level (Mio ECU)</th>
<th>Calendar/other year applied (*)</th>
<th>Annual and final outlay commitment levels 1995 – 2000 (Mio ECU)</th>
<th>Base Quantity (**)</th>
<th>Calendar/other year applied (*)</th>
<th>Annual and final quantity commitment levels 1995 – 2000 (000 t)</th>
<th>Relevant Supporting Tables and document reference</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1</td>
<td>2</td>
<td>3</td>
<td>4</td>
<td>5</td>
<td>6</td>
<td>7</td>
</tr>
<tr>
<td>Sugar (1)</td>
<td>779.9</td>
<td>733.1</td>
<td>686.3</td>
<td>639.5</td>
<td>592.7</td>
<td>545.9</td>
<td>499.1</td>
</tr>
</tbody>
</table>

(* ) See Annex

(1) Does not include exports of sugar of ACP and Indian origin on which the Community is not making any reduction commitments. The average of export in the period 1986 to 1990 amounted to 1.6 mio t.

Note: For the purpose of this Panel Report, references to products other than sugar have been deleted from this page of the European Communities' Schedule.
EUROPEAN COMMUNITIES – EXPORT SUBSIDIES ON SUGAR

Request for the Establishment of a Panel by Australia

The following communication, dated 9 July 2003, from the Permanent Mission of Australia to the Chairman of the Dispute Settlement Body, is circulated pursuant to Article 6.2 of the DSU.

My authorities have requested me to submit the following request for the establishment of a panel on behalf of Australia.

On 27 September 2002 Australia requested consultations with the European Communities (EC) pursuant to Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (DSU), Article XXII:1 of the General Agreement on Tariffs and Trade 1994 (GATT 1994), Article 19 of the Agreement on Agriculture and Articles 4 and 30 of the Agreement on Subsidies and Countervailing Measures (SCM Agreement) with respect to the EC's Common Organization of the Markets in sugar and its application and implementation. The request was circulated to Members on 1 October 2002 in document number WT/DS265/1. Consultations were held on 21 and 22 November 2002 but unfortunately did not result in resolution of the dispute.

Consequently, Australia requests that a Panel be established pursuant to Article 4.7 and Article 6 of the DSU, Article XXIII:2 of GATT 1994, Article 19 of the Agreement on Agriculture and Article 4.4 and Article 30 of the SCM Agreement.

The measures that are the subject of this request are the subsidies provided by the EC in excess of its reduction commitment levels on sugar and sugar containing products including sugar cane and sugar beet, processed and unprocessed cane and beet sugar and chemically pure sucrose in solid form, molasses resulting from the extraction of refining of sugar, isoglucose, inulin syrup and the other products listed in Article 1 of Council Regulation (EC) No 1260/2001 of 19 June 2001 on the European Communities' Common Organization of the markets in sugar sector (Official Journal of the European Communities, 30 June 2001, L178/1-45).

The above-mentioned subsidies are accorded through the EC sugar regime, which is contained in a number of EC regulations including Council Regulation No 1260/2001 and related EC
regulations, administrative policies, rules, decisions and other instruments including instruments pre-
dating the above regulation, and their implementation. These various instruments will be referred to as "the EC sugar regime".

In addition to setting down the conditions attaching to imports of sugar, the EC sugar regime
provides conditions attached to the production, supply and exports of sugar, including domestic
support and export subsidies. Sugar is classified into quota and non-quota sugar. Non-quota sugar is
known as C sugar. The sugar regime provides for the reclassification from quota to C sugar and from
C sugar to quota sugar. Sugar classified as C sugar cannot be disposed of in the EC market.

Australia is particularly concerned at the subsidies provided by the EC for "C sugar" exports
under the EC sugar regime. Under the regime, producers of C sugar are able to sell C sugar on the
world market at below the total average cost of production through cross-subsidisation of C sugar
from quota sugar profits. By financing payments on the export of C sugar, the EC exceeds its export
subsidy reduction commitments under the WTO Agreement on Agriculture.

Australia is also particularly concerned at the provisions of the EC sugar regime which accord
direct subsidies contingent on export performance for quantities of approximately 1.6 million tonnes
of sugar which are additional to the budgetary outlays and quantities of subsidised exports notified by
the EC to the Committee on Agriculture under the provisions of Article 18.2 of the Agreement on
Agriculture. In the application of those provisions, the EC significantly exceeds its budgetary outlays
and quantity commitments for export subsidies on sugar under the Agreement on Agriculture.

By granting export subsidies within the meaning of Articles 1.1(a)(1)(i), 1.1(a)(1)(iv),
1.1(a)(2) and 1.1(b) of the SCM Agreement that are not permitted by the Agreement on Agriculture,
the EC also acts inconsistently with its obligations under Articles 3.1(a) and 3.2 of the SCM
Agreement.

Australia considers that the provision of the above subsidies and the relevant elements of the
EC sugar regime are inconsistent with the EC's obligations under the following provisions:

– Articles 3.3, 8, 9.1(a), 9.1(c), and alternatively, 10.1 of the Agreement on Agriculture;
– Articles 3.1(a) and 3.2 of the Agreement on Subsidies and Countervailing Measures.

Australia therefore requests the establishment of a Panel in accordance with Article 7 of the
DSU.

I would be grateful if you would place this item on the agenda for the next DSB meeting
scheduled for 21 July 2003.
The following communication, dated 9 July 2003, from the Permanent Mission of Brazil to the Chairman of the Dispute Settlement Body, is circulated pursuant to Article 6.2 of the DSU.

On 27 September 2002, Brazil requested consultations with the European Communities ("EC") pursuant to Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"), Article XXII:1 of the General Agreement on Tariffs and Trade 1994 ("GATT 1994"), Article 19 of the Agreement on Agriculture, and Articles 4.1 and 30 of the Agreement on Subsidies and Countervailing Measures ("SCM Agreement"), with respect to export subsidies provided by the EC to its sugar industry. That request was circulated to Members in document WT/DS266/1, G/L/570, G/AG/GEN/53, G/SCM/D48/1, dated 1 October 2002. Consultations were held in Geneva on 21 and 22 November 2002, with a view to reaching a mutually satisfactory solution. Unfortunately, these consultations failed to resolve the dispute.

Therefore, pursuant to Articles 4.7, 6 and 7 of the DSU, Article 19 of the Agreement on Agriculture, Articles 4.4 and 30 of the SCM Agreement, and Article XXIII:2 of the GATT, Brazil hereby requests the establishment of a panel.

The specific measures at issue in this dispute are the subsidies provided and maintained by the EC, in excess of the EC's reduction commitment levels for sugar, under Council Regulation (EC) No. 1260/2001 of 19 June 2001 on the European Communities' common organization of the markets in the sugar sector, and pursuant to all other legislation, regulations, administrative policies and other instruments relating to the EC regime for sugar, including the rules adopted pursuant to the procedure referred to in Article 42(2) of Council Regulation (EC) No. 1260/2001 of 19 June 2001, and any other provision related thereto. These are referred to as the "EC sugar regime". The products at issue are those listed in Article 1 of the Regulation, including cane or beet sugar and chemically pure sucrose in solid form, molasses resulting from the extraction or refining of sugar, isoglucose and inulin syrup. These products are referred to collectively as "sugar".

The EC provides export subsidies for sugar in excess of its reduction commitment levels specified in Section II of Part IV of its Schedule of Concessions (Schedule CXL-European Community Sugar).
Communities), in violation of the Agreement on Agriculture and the SCM Agreement. In particular, Brazil is concerned with two categories of subsidized EC exports:

(i) The EC sugar regime guarantees a high price for the sugar that is produced within production quotas. This is termed "A and B sugar". Sugar produced in excess of these quotas is termed "C sugar". Sugar classified as C sugar cannot be sold internally in the year in which it is produced, and must, in principle, be exported. Payments in the form of high prices provided to growers and processors by the EC sugar regime finance the production and export of C sugar at prices below its total cost of production.

(ii) The EC grants export subsidies to an amount of white sugar ostensibly equivalent to the quantity of raw sugar that the EC imports under its preferential arrangements. This amount, reportedly, is approximately 1.6 million tons.

The EC unjustifiably excludes these subsidies from the calculation of its total amount of export subsidies that it provides for sugar. The amount of sugar thus subsidized, alone or in combination with other export subsidies for sugar provided by the EC, exceeds the export subsidy reduction commitment levels and, as such, constitutes a violation of the EC’s obligations under Articles 3.3, 8, 9.1 (a) and (c), or, alternatively, Article 10.1 of the Agreement on Agriculture. By granting export subsidies within the meaning of Articles 1.1(a)(1)(i) and (iv), 1.1(a)(2), and 1.1(b) of the SCM Agreement, that are not permitted by the Agreement on Agriculture, the EC also acts inconsistently with its obligations under Articles 3.1(a) and 3.2 of the SCM Agreement.

Brazil asks that this request for the establishment of a panel be placed on the agenda of the next meeting of the Dispute Settlement Body, which is scheduled to take place on 21 July 2003.
EUROPEAN COMMUNITIES – EXPORT SUBSIDIES ON SUGAR

Request for the Establishment of a Panel by Thailand

The following communication, dated 9 July 2003, from the Permanent Mission of Thailand to the Chairman of the Dispute Settlement Body, is circulated pursuant to Article 6.2 of the DSU.

On 14 March 2003, pursuant to Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes (the "DSU"), Article XXIII of the General Agreement on Tariffs and Trade 1994 (the "GATT 1994"), Article 19 of the Agreement on Agriculture, and Articles 4 and 30 of the Agreement on Subsidies and Countervailing Measures (the "SCM Agreement") the Kingdom of Thailand ("Thailand") requested consultations with the European Communities (the "EC") with respect to export subsidies provided by the EC in the sugar sector. The request was circulated to Members on 20 March 2003 in document WT/DS283/1. The EC and Thailand held consultations in Geneva on 8 April 2003 with a view to reaching a mutually satisfactory resolution of the matter, but failed to resolve the dispute. Pursuant to Articles 4.7 and 6 of the DSU, Article XXIII:2 of the GATT 1994, Article 19 of the Agreement on Agriculture and Articles 4.4 and 30 of the SCM Agreement, Thailand therefore requests the Dispute Settlement Body (the "DSB") to establish a panel to examine the following matter.

The measures at issue are the export subsidies for sugar and sugar-containing products accorded under Council Regulation (EC) No. 1260/2001 of 19 June 2001 on the common organization of the markets in the sugar sector published in the Official Journal of the European Communities on 30 June 2001 (L 178/1-45) and related legal instruments. The Council Regulation and the related legal instruments and administrative actions will be referred to below as the "EC sugar regime". The products at issue are those listed in Article 1 of the Council Regulation, including cane or beet sugar and chemically pure sucrose in solid form, molasses resulting from the extraction or refining of sugar, isoglucose and inulin syrup. These products will be referred to below as "sugar".

Under the EC sugar regime, sugar that is produced within production quotas ("A" and "B" quotas) is guaranteed a high intervention price. Sugar produced in excess of those quotas ("C-sugar") must in principle be exported. By virtue of the EC sugar regime, exporters of C-sugar are able to export such sugar at prices below the average cost of production. The EC therefore accords export subsidies to C-sugar in the form of payments on the export of sugar financed by virtue of governmental action.
Furthermore, under its sugar regime, the EC grants export refunds to an amount of white sugar that the EC claims to be equivalent to the quantity of raw sugar imported under preferential import arrangements. The export refunds cover the difference between the world market price and the high prices in the EC for the products in question, thus making it possible for those products to be exported. The export refunds constitute direct subsidies contingent on export performance.

Under the Agreement on Agriculture, the EC undertook budgetary outlay and export quantity reduction commitments with respect to sugar. In determining its budgetary outlays for export subsidies for sugar and the quantities benefiting from such subsidies, the EC does not take into account exports of C-sugar and exports of an amount of white sugar equivalent to the quantity of raw sugar imported under preferential import arrangements. As a result, the EC provides export subsidies for sugar in excess of its reduction commitments and consequently acts inconsistently with its obligations under Articles 3.3, 8, 9.1(a) and 9.1(c) of the Agreement on Agriculture or, alternatively, Article 10.1 of the Agreement on Agriculture. By granting export subsidies within the meaning of Articles 1.1(a)(1)(i) and (iv), 1.1(a)(2), and 1.1(b) of the SCM Agreement, that are not permitted by the Agreement on Agriculture, the EC also acts inconsistently with its obligations under Articles 3.1(a) and 3.2 of the SCM Agreement.

I would appreciate it if this request for the establishment of a panel were placed on the agenda for the meeting of the DSB scheduled for 21 July 2003.