ANNEX D

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

ANNEX D-1

BRAZIL'S REQUEST FOR THE PANEL TO SEEK PRODUCTION OF DOCUMENTS AND INFORMATION PURSUANT TO ARTICLE 13 OF THE DSU

(1 November 2006)

1. The Government of Brazil would like to thank you, as well as Ambassador Ahn and Ambassador Matus, for agreeing to serve as panelists in *United States - Subsidies on Upland Cotton (Recourse by Brazil to Article 21.5 of the DSU).* We appreciate your willingness to devote time and energy to assisting Brazil and the United States to resolve this matter. Brazil also looks forward to providing you, the panelists and the Secretariat with whatever assistance it can in these proceedings.

2. In this letter, Brazil seeks that the compliance Panel exercise its discretion under Article 13.1 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU")[1] to request the United States to produce documents and information relating to (a) payments to U.S. producers of upland cotton under the U.S. counter-cyclical payment program established by the FSRI Act of 2002, and (b) the U.S. agricultural export credit guarantee programs (principally the General Sales Manager 102 ("GSM 102") export credit guarantee program). **Annex 1** to this letter sets out the precise documents and information that Brazil requests the Panel to seek from the United States.

3. All of the documents and information sought by Brazil is within the exclusive control of the United States. All of it is highly relevant to Brazil's claims and the issues before this compliance Panel. Therefore, Brazil considers that it is "necessary and appropriate" for the compliance Panel to seek the documents and information requested at this early stage of the compliance proceeding. Doing so is also "necessary and appropriate" given the shortened timeframe for the panel procedure, provided for in Article 21.5 of the DSU, and in light of the importance accorded to this information by the panel in the original proceeding.

4. Prior to making this request, Brazil sought to secure the agreement of the United States to produce this information.

5. **Annex 2a** to this letter contains Brazil's letter, dated 7 June 2006, requesting informal discussions on the U.S. implementation of the recommendations and rulings of the Dispute Settlement Body in this dispute; **Annex 2b** contains the questions presented by Brazil prior to and during the informal discussions on this matter on 19 July 2006.

6. In the few instances in which the United States provided documents or information during the informal discussions, Brazil has not repeated the question in Annex 1 to this letter. For the majority of the documents and information requested by Brazil, the United States indicated during the informal discussions that it was not in a position to produce the documents or information. Nor has the United States subsequently offered to produce the requested documents or information. During those discussions, the United States indicated that at least part of the documents or information requested

[1] Article 13.1 provides, in relevant part: "Each panel shall have the right to seek information . . . from any individual or body which it deems appropriate. . . . 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 or the Member providing the information."

was confidential and that it was not prepared to provide them in the context of discussions not formally protected by confidentiality. The United States added that the situation would be different if such request was presented during panel proceedings which, pursuant to Article 18 of the DSU, take place under a confidentiality clause.

7. Brazil and its representatives also made requests seeking these documents and information under the U.S. Freedom of Information Act ("FOIA"). In most instances, Brazil has not received documents or information pursuant to those FOIA requests. In the few instances in which Brazil received documents or information in response to those FOIA requests, relevant questions have been eliminated from Annex 1 to this letter.

8. Brazil sets out the requested documents and information regarding the U.S. **counter-cyclical payment** program in Part A of Annex 1. This request is essentially *identical* to the original panel's final request to the United States pursuant to Article 13.1 of the DSU.[2] The United States eventually provided considerable data to the original panel in response to this request. The relevant background concerning the original panel's final request (as well as previous requests) under Article 13.1 of the DSU is set out in paragraphs 7.20-7.42 of the Panel Report in *United States - Subsidies on Upland Cotton.*

9. That data produced by the United States allowed the original panel to make an assessment of both the amount and type of counter-cyclical payments received by current upland cotton producers. For the reasons set out below, it is "necessary and appropriate" for the compliance Panel to exercise its discretion, under Article 13.1 of the DSU, to request the United States to produce an update of this same data.

10. Brazil recalls that the original panel found that the "support delivered to upland cotton by [counter-cyclical payments] is a central issue in this dispute."[3] Using the information on counter-cyclical payments obtained from the United States in response to its Article 13.1 request, the original panel made extensive findings of fact.[4] For example, the original panel found that "the overwhelming majority of farms enrolled in the programmes which plant upland cotton also hold upland cotton base."[5] The original panel further found that the data produced by the United States

> *show a strongly positive relationship between those recipients who hold upland cotton base acres and those who continue to plant upland cotton, despite their entitlement to plant other crops, which is indicative of the relationship between payments calculated with respect to upland cotton base acreage and recipients who plant upland cotton.*[6]

In addition, the original panel found that the magnitude of the price-contingent counter-cyclical payments received by current producers of upland cotton ($869.4 million using Brazil's Methodology, or $864.9 using the Cotton-to-Cotton methodology[7]) constituted "very large amounts of United States government money benefiting United States upland cotton production."[8]

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[2] Panel Report, *United States - Subsidies on Upland Cotton*, Annexes L-1.22, dated 3 February 2004, and L-1.23, dated 16 February 2004.

[3] Panel Report, *United States - Subsidies on Upland Cotton*, para. 7.633.

[4] *See, inter alia*, Panel Report, *United States - Subsidies on Upland Cotton*, paras. 7.608-7.633 and 7.634-7.647.

[5] Panel Report, *United States - Subsidies on Upland Cotton*, para. 7.636.

[6] Panel Report, *United States - Subsidies on Upland Cotton*, para. 7.637.

[7] Panel Report, *United States - Subsidies on Upland Cotton*, Tables A-5, A-6, paras. 7.641-7.647.

[8] Panel Report, *United States - Subsidies on Upland Cotton*, para. 7.1349.

11. Before the compliance Panel, a central question will be whether the failure of the United States to withdraw, or remove the adverse effects of, the counter-cyclical payment program of the FSRI Act of 2002 causes present serious prejudice to the interests of Brazil, or a threat thereof. The existence and strength of a causal link between counter-cyclical payments and serious prejudice is, in part, a function of the magnitude and type of counter-cyclical payments received by current producers of upland cotton. Thus, the magnitude and type of these subsidies continues to be a central issue. As in the original panel proceeding, the data requested by Brazil would constitute the basis for factual findings regarding the magnitude and type of countercyclical payments that continue to support the production and export of U.S. upland cotton.

12. Publicly-available USDA data shows that, in marketing year ("MY") 2005 for example, total counter-cyclical payments to holders of upland cotton base acreage exceeded $1.3 billion. While USDA collects data on plantings of each recipient that allow the calculation of the amount of counter-cyclical payments that were received annually by current upland cotton farmers, these data are not publicly available. They are therefore not available to Brazil or the compliance Panel. Significantly, during the original proceedings, the United States produced these data for MY 2002. The original panel relied on certain methodologies of using the data to calculate the amount of counter-cyclical subsidies received by current U.S. upland cotton farmers for MY 2002.[9]

13. Wile awaiting the production of the requested data by the United States, Brazil, based on the best information currently available to it and the compliance Panel, intends to rely on the methodology found "appropriate" by the original panel.

14. Brazil sets out its questions with respect to the **agricultural export credit guarantee ("ECG") programs, and in particular, the GSM 102 program**[10], in Part B of Annex 1 to this letter. Brazil notes that it has considerably reduced the number of questions compared to those originally requested prior to and during the 19 July 2006 informal discussions. Brazil was able to obtain some of the originally requested documents through FOIA requests, and has taken account of limited responses from the United States in informal discussions on 19 July. (The United States provided no *documents* in connection with these informal discussions.)

15. The documents and information regarding export credit guarantees requested in Annex 1 are exclusively within the control of the United States. The majority of the questions seek documents and information concerning the risk profile of the GSM 102 portfolio, how GSM 102 takes the various risks encountered in guaranteed transactions into account, and default rates on GSM 102 guarantees. The requested documents and information will help the compliance Panel fulfill its mandate to undertake an objective assessment of the United States' ECG-related measures taken to comply, and to consider Brazil's claims that GSM 102 guarantees constitute export subsidies, as well as that they circumvent U.S. agricultural export subsidy commitments. Brazil believes, therefore, that it is "necessary and appropriate" for the compliance Panel to exercise its discretion under Article 13.1 of the DSU, and to request this information from the United States.

16. Finally, Brazil asks the compliance Panel to request the United States to produce this information within three weeks of the date the Panel issues its request.[11] Brazil considers this time period is justified in view of the shortened timeframe provided for in Article 21.5 of the DSU. It is also consistent with the relative importance of the information requested.

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[9] Panel Report, *United States - Subsidies on Upland Cotton,* Attachment to Section VII:D, paras. 7.634-7.647.

[10] Brazil notes that one questions relates also to the GSM 103 and Supplier Credit Guarantee programs.

[11] Brazil recalls that the original panel allotted the United States eight days (until 11 February 2004) to respond to its 3 February 2004 request for information. *See,* Panel Report, *United States - Subsidies on Upland Cotton,* Annex I-1.22.

ANNEX 1

Brazil's Request to the Compliance Panel to Pose Questions to the United States, under Article 13.1 of the DSU

1 November 2006

Part A: Documents and Information on Base and Planted Acres

1. Brazil requests updated information on upland cotton planted and base acres under the Direct and Counter-Cyclical Payment Program for each of the **2003, 2004, 2005 and 2006 marketing years**, showing as many of the underlying calculations as possible. Brazil also requests information on base acreage and planted acreage for other "program crops" (*i.e.*, corn, barley, oats, sorghum, rice, wheat, soybeans, peanuts and minor oilseeds) and other acreage on farms with upland cotton planted acreage in these same years. Finally, Brazil requests the amount of payments units for Direct Payments and Counter-Cyclical Payments by program crop for each category of farms.

Brazil requests this information in the format outlined by the Panel in part (b) of its "Supplementary Request for Information Pursuant to Article 13 of the DSU," dated 3 February 2004.[1] Specifically, Brazil requests that the United States address the following questions:

(A) How many farms that planted upland cotton had fewer upland cotton planted acres than upland cotton base acres, or equal numbers of each? We refer to these as "Category A" farms. What was the total of their upland cotton base acreage? What was the total of their upland cotton planted acreage?

(1) How many farms that have upland cotton base acres did not plant any upland cotton? What was the total upland cotton base acreage on these farms? We refers to these as "Category A-1" farms.[2]

(B) How many farms had more upland cotton planted acres than upland cotton base acres? We refer to these as "Category B" farms. What was the total of their base acreage for each covered commodity, including upland cotton? What was the total of their planted acreage for each covered commodity, including upland cotton? Please also provide the following information concerning these farms:

(1) How many Category B farms had equal numbers of acres planted to all covered commodities and base acres for all covered commodities? We refer to these as "Category B-1" farms. What was the total of the base acreage of Category B-1 farms for each covered commodity, including upland cotton? What was the total of the planted acreage

[1] Panel Report, Annex L, item 22. The Panel's request for information is contained in the Communication from the Panel on 3 February 2004. The full Communication (Panel Report, Annex L, item 22) is attached in Appendix I of this document.

[2] For Category A Farms, the Panel requested "farms [that] had fewer upland cotton planted acres than upland cotton base acres." (*See Panel Report, Annex L, item 22, p. 2*).[2] The United States interpreted this request as covering all farms that had upland cotton base and planted less than their full upland cotton base to upland cotton or that planted no upland cotton at all. (*The full response by the United States is attached in Appendix II of this document*). In its updated request, Brazil would like the United States to separate (i) farms that had upland cotton base acres and planted *fewer* upland cotton planted acres than upland cotton base acres and (ii) farms that had upland cotton base acres but planted *no* upland cotton. *(See also Panel Report, Annex L, item 26, para. 5*)

of Category B-1 farms for each covered commodity, including upland cotton?

(2) How many Category B farms had fewer acres planted to all covered commodities than base acres for all covered commodities? We refer to these as "Category B-2" farms. How much was the total acreage of Category B-2 farms planted to all covered commodities less than their base acreage for all covered commodities? What was the total of the base acreage of Category B-2 farms for each covered commodity, including upland cotton? What was the total of the planted acreage of Category B-2 farms for each covered commodity, including upland cotton?

(3) How many Category B farms had more acres planted to all covered commodities than base acres for all covered commodities? We refer to these as "Category B-3" farms. How much did the total acreage of Category B-3 farms planted to all covered commodities exceed their base acreage for all covered commodities? What was the total of the base acreage of Category B-3 farms for each covered commodity, including upland cotton? What was the total of the planted acreage of Category B-3 farms for each covered commodity, including upland cotton?

(C) How many farms had upland cotton planted acres but no upland cotton base acres? We refer to these as "Category C" farms. What was the total of the base acreage of Category C farms for each covered commodity? What was the total of the planted acreage of Category C farms for each covered commodity, including upland cotton?

(D) In addition, for the marketing years 2003 through 2006, please reply to the above questions with respect to all crops on cropland covered by the acreage reports, not simply commodities covered by the programs.

Brazil requests that the United States continue to provide the requested information on both state level and federal level (*i.e.*, totals). Further, as noted above, Brazil requests that the United States provide aggregate payment unit data by crop for each group of farms.

For convenience, Brazil attaches the Panel's communication dated 3 March 2004, which contains the Panel's "Supplementary Request for Information Pursuant to Article 13 of the DSU," in Appendix I to this document. Brazil further attaches, in Appendix II to this document, an excerpt of the U.S. response to the Panel's data request, dated 3 March 2004.

Part B: Documents and Information on Export Guarantee Programs

2. In the original panel proceedings in WT/DS267, the United States provided, as Exhibit US-150, two memoranda, dated 8 April 2002 and 25 March 2003, titled "Annual Review of Fees for USDA Credit Programs". Please provide any memoranda or similar documents constituting annual reviews for subsequent years.

3. What return does the U.S. government require on capital employed for the GSM 102 program?

4. Please provide data regarding the value of GSM 102 guaranteed transactions, by tenor and by country (rather than by Commodity Credit Corporation ("CCC") regional groupings)[3], for the cohort of GSM 102 guarantees issued in each fiscal year for FY 2002-2006.

5. For FY 2006, please separate GSM 102 ECGs into applications received by individual country (rather than by CCC regional groupings).[4]

6. Please provide data regarding GSM 102 fees collected, by country (rather than by CCC regional groupings), by year for each of FY 2002-2006.[5]

7. For each country eligible for export credit guarantees through the GSM 102 program, please provide the current sovereign-risk rating and the private risk-rating established through the Interagency Country Risk Assessment System ("ICRAS"), as well as any ICRAS papers or analyses justifying those ratings. Please provide the same information and documents for FY 2002-2006, to the extent ratings in that period diverge from current ratings.

8. Please indicate the number of risk categories into which CCC classifies guarantees for the GSM 102 program, and explain: (i) how those risk categories are established; and (ii) how those risk categories correspond to the ICRAS categories.

9. Whether CCC uses the ICRAS risk categories or its own risk categories, please:

(a) provide a correspondence table and documentary support showing the correspondence between the CCC risk categories and the ratings (*e.g.*, BB, BBB, BBB-, etc.) in the Moody's or Standard and Poor's rating systems;

(b) for FY 2002-2006, indicate the value of guaranteed transactions in each CCC risk category for GSM 102 guarantees issued in each of those years;

(c) for FY 2005 and 2006, indicate the value of guaranteed transactions in each CCC risk category for the portfolio of GSM 102 guarantees outstanding on the last day of each fiscal year;

10. For the cohort of GSM 102 guarantees issued in each of FY 2002-2006, please provide data dividing the cohort according to the value of the transactions guaranteed. Please use increments of $1000.

11. For the cohort of GSM 102 guarantees issued in each of FY 2002-2006, please provide data dividing the cohort according to the credit rating of the foreign bank.

12. For the cohort of GSM 102 guarantees issued in each of FY 2002-2006, please provide data dividing the cohort according to the credit rating of the foreign purchaser of U.S. agricultural exports.

13. For the cohort of GSM 102 guarantees issued in each of fiscal years 2002-2006, please provide data dividing the cohort according to the value of the transactions guaranteed, and, further, indicates loss or default rates for each $1000 increment of transaction value.

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[3] Monthly exposure reports for GSM 102 demonstrate that CCC maintains data on a country-specific basis.

[4] Monthly exposure reports for GSM 102 demonstrate that CCC maintains data on a country-specific basis.

[5] Monthly exposure reports for GSM 102 demonstrate that CCC maintains data on a country-specific basis.

14. Please provide data and documentary support addressing default rates for the GSM 102 program for each fiscal year during the period 2002-2006.

15. For each country eligible for export credit guarantees through the GSM 102 program, please provide the Office of Management and Budget's (OMB) default estimate.[6]

16. With respect to the total amount of outstanding principal and interest guaranteed through GSM 102, GSM 103 and SCGP on 1 July 2005:

(a) What proportion of that outstanding principal and interest was associated with exports of unscheduled products, and what proportion was associated with exports of scheduled products?

(b) Of the proportion associated with scheduled products, what proportion was associated with exports of rice?

17. Please provide monthly "Exposure Reports" for GSM 102 all months beginning in July of FY 2006.[7]

18. Please provide the "FAS Risk Assessment Handbook".[8]

19. Please provide any "FAS Portfolio Analysis" of the export credit guarantee programs conducted and/or reported subsequent to 24 March 2003.[9]

20. Please provide the quarterly "Commercial Export Credit Reports" for all quarters from Q2 of FY 2004 to the present.[10]

21. Please provide the quarterly "Geographic and Commodity Analyses" for all quarters from FY 2002 to the present.[11]

22. Please provide the quarterly "FAS GSM to Exports Powerpoints" from Q3 of FY 2004 to the present.[12]

23. Please provide the "Contingent Liability by Country Risk Grade Powerpoints" from FY 2002 to the present.[13]

[Appendix 1 and Appendix 2 omitted.]

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[6] OMB's default estimate methodology is discussed on page 79 of the "Analytical Perspectives" document associated with the U.S. 2007 budget, available at http://www.whitehouse.gov/omb/budget/fy2007/.

[7] Cited as "evidence" in an OMB assessment of the ECG programs, available at http://www.whitehouse.gov/omb/expectmore/detail.10002020.2005.html.

[8] Cited as "evidence" in an OMB assessment of the ECG programs, available at http://www.whitehouse.gov/omb/expectmore/detail.10002020.2005.html.

[9] Cited as "evidence" in an OMB assessment of the ECG programs, available at http://www.whitehouse.gov/omb/expectmore/detail.10002020.2005.html.

[10] Cited as "evidence" in an OMB assessment of the ECG programs, available at http://www.whitehouse.gov/omb/expectmore/detail.10002020.2005.html.

[11] Cited as "evidence" in an OMB assessment of the ECG programs, available at http://www.whitehouse.gov/omb/expectmore/detail.10002020.2005.html.

[12] Cited as "evidence" in an OMB assessment of the ECG programs, available at http://www.whitehouse.gov/omb/expectmore/detail.10002020.2005.html.

[13] Cited as "evidence" in an OMB assessment of the ECG programs, available at http://www.whitehouse.gov/omb/expectmore/detail.10002020.2005.html.

ANNEX 2a

**BRAZIL'S LETTER OF 7 JUNE 2006
TO THE UNITED STATES**

The Government of Brazil is concerned that measures taken by the United States to comply with the recommendations and rulings adopted by the WTO Dispute Settlement Body ("DSB) on 21 March 2005 in *United States - Subsidies on Upland Cotton* (DS 267) may not exist or not be consistent with the U.S. obligations under the *Dispute Settlement Understanding,* the *Agreement on Subsidies and Countervailing Measures* and the *Agreement on Agriculture.* In particular, the Government of Brazil believes that it would be useful to hold further substantive discussions concerning ongoing and future efforts by the U.S. Government to eliminate or make significant changes to the marketing loan and countercyclical programs for upland cotton under the Farm Security and Rural Investment Act of 2002, as well as the GSM 102 and SCGP export credit guarantee programs.

Therefore, the Government of Brazil suggests that informal contacts be held at your earliest convenience to provide an opportunity to exchange views and information regarding the above-mentioned concerns. To prepare for this meeting, and in order to facilitate the discussions, Brazil would send in advance a list of questions that could be addressed during the talks. I look forward to your response to this suggestion.

Please accept, Excellency, the assurances of my highest consideration.

ANNEX 2b

**BRAZIL'S LETTER OF 29 JUNE 2006
TO THE UNITED STATES**

With reference to your letter of 23 June 2006 confirming the disposition of the United States to discuss with Brazil issues related to the implementation of the Dispute Settlement Body's ("DSB") rulings and recommendations in the context of the dispute *United States - Subsidies on Upland Cotton* (DS 267), I would like to propose that representatives of our countries meet on **17 July 2006** in Geneva.

As anticipated in my letter of 7 June 2006, and with a view to ensuring that this exchange of views and information be as valuable and informative as possible, please find enclosed a list of questions.

Please accept, Excellency, the assurances of my highest consideration.

Questions for the United States
29 June 2006

Information on the Amount of Step 2 Payments by Marketing Year

1. Brazil requests information on the annual amount of user marketing (Step 2) payments for upland cotton in marketing years 2002-2005. Brazil requests separate data for Step 2 export payments and Step 2 payments for domestic users.

Information on the United States' Intention to Take Further Implementing Action

2. Does the United States intend to change the Counter-Cyclical Payment Program and/or Marketing Loan Program to bring them/it into conformity with U.S. WTO obligations? If so, what is the envisioned outline and time-frame of such changes. If not, please provide a reasoned and substantiated explanation of why it believes that no further implementing action is needed to comply with the DSB's rulings and recommendations in *United States – Subsidies on Upland Cotton*.

Information on Base and Planted Acres

3. Brazil requests updated information on upland cotton planted and base acres under the Direct and Counter-Cyclical Payment Program for each of the **marketing years 2003, 2004, 2005 and 2006**[1]**,** showing as many of the underlying calculations as possible. Brazil also requests information on base acreage and planted acreage for other "program crops" (*i.e.*, corn, barley, oats, sorghum, rice, wheat, soybeans, peanuts and minor oilseeds) and other acreage on farms with upland cotton planted acreage in these same years. Finally, Brazil requests the amount of payments units for Direct Payments and Counter-Cyclical Payments by program crop for each category of farms.

Brazil requests this information in the format outlined by the Panel in part (b) of its "Supplementary Request for Information Pursuant to Article 13 of the DSU," dated 3 February 2004.[2] Specifically, Brazil requests that the United States address the following questions:

(A) How many farms that planted upland cotton had fewer upland cotton planted acres than upland cotton base acres, or equal numbers of each? We refer to these as "Category A" farms. What was the total of their upland cotton base acreage? What was the total of their upland cotton planted acreage?

(1) How many farms that have upland cotton base acres did not plant any upland cotton? What was the total upland cotton base acreage on these farms? Brazil refers to these as "Category A-1" farms.[3]

[1] Brazil understands that information on marketing year 2006 may be preliminary or incomplete.

[2] Panel Report, Annex L, item 22. The Panel's request for information is contained in the Communication from the Panel on 3 February 2004. The full Communication (Panel Report, Annex L, item 22) is attached in Annex I of this document.

[3] For Category A Farms, the Panel requested "farms [that] had fewer upland cotton planted acres than upland cotton base acres." (*See Panel Report, Annex L, item 22, p. 2*).[3] The United States interpreted this request as covering all farms that had upland cotton base and planted less than their full upland cotton base to upland cotton or that planted no upland cotton at all. (*The full response by the United States is attached in Annex II*). In its updated request, Brazil would like the United States to separate (i) farms that had upland cotton base acres and planted *fewer* upland cotton planted acres than upland cotton base acres and (ii) farms that had upland cotton base acres but planted *no* upland cotton. *(See also Panel Report, Annex L, item 26, para. 5*)

(B) How many farms had more upland cotton planted acres than upland cotton base acres? We refer to these as "Category B" farms. What was the total of their base acreage for each covered commodity, including upland cotton? What was the total of their planted acreage for each covered commodity, including upland cotton? Please also provide the following information concerning these farms:

(1) How many Category B farms had equal numbers of acres planted to all covered commodities and base acres for all covered commodities? We refer to these as "Category B-1" farms. What was the total of the base acreage of Category B-1 farms for each covered commodity, including upland cotton? What was the total of the planted acreage of Category B-1 farms for each covered commodity, including upland cotton?

(2) How many Category B farms had fewer acres planted to all covered commodities than base acres for all covered commodities? We refer to these as "Category B-2" farms. How much was the total acreage of Category B-2 farms planted to all covered commodities less than their base acreage for all covered commodities? What was the total of the base acreage of Category B-2 farms for each covered commodity, including upland cotton? What was the total of the planted acreage of Category B-2 farms for each covered commodity, including upland cotton?

(3) How many Category B farms had more acres planted to all covered commodities than base acres for all covered commodities? We refer to these as "Category B-3" farms. How much did the total acreage of Category B-3 farms planted to all covered commodities exceed their base acreage for all covered commodities? What was the total of the base acreage of Category B-3 farms for each covered commodity, including upland cotton? What was the total of the planted acreage of Category B-3 farms for each covered commodity, including upland cotton?

(C) How many farms had upland cotton planted acres but no upland cotton base acres? We refer to these as "Category C" farms. What was the total of the base acreage of Category C farms for each covered commodity? What was the total of the planted acreage of Category C farms for each covered commodity, including upland cotton?

(D) In addition, for the marketing years 2003 through 2006, please reply to the above questions with respect to all crops on cropland covered by the acreage reports, not simply commodities covered by the programs.

Brazil requests that the United States continue to provide the requested information on both state level and federal level (*i.e.*, totals). Further, as noted above, Brazil requests that the United States provide aggregate payment unit data by crop for each group of farms.

For the United States' convenience, Brazil attaches the Panel's communication dated 3 March 2004, which contains the Panel's "Supplementary Request for Information Pursuant to Article 13 of the DSU," in Annex I. Brazil further attaches, in Annex II, an excerpt of the U.S. response to the Panel's data request, dated 3 March 2004.

Information on the General Sales Manager 102 (GSM 102), General Sales Manager 103 (GSM 103) and Supplier Credit Guarantee (SCGP) Programs

4. In a press release dated 5 July 2005, USDA announced that the Bush Administration was sending to Congress proposed statutory changes to remove the one-percent cap on fees for guarantees issued under the GSM 102 and SCGP programs (the one-percent fee cap is required by 7 U.S.C. § 5641(b)(1)), and terminate the Intermediate Export Guarantee Program (GSM-103).[4] In a paper dated 17 February 2006 and titled "WTO Litigation and Negotiation: Potential Implications for Cotton", at page 2, Carol Goodloe, Senior Economist in USDA's Office of the Chief Economist, suggested that the proposal to repeal the fee cap and to eliminate the GSM-103 program was not "included" in budget reconciliation legislation because of "Senate rules".[5]

With respect to this issue, Brazil has the following questions:

(a) Was the 2005 Administration proposal not "included" in budget reconciliation legislation because of "Senate rules"? If yes, please explain the nature of the Senate rules. If not, please explain why the proposal was not "included" in budget reconciliation legislation.

(b) Please provide a copy of any subsequent legislative proposals concerning repeal of the fee cap or termination of GSM-103 program provided by the Executive Branch to the US Congress. What is the legislative vehicle and timeline for consideration and adoption of these proposals?

(c) Does the United States expect that the Congress will vote on an FY 2007 budget reconciliation bill in calendar year 2006? Please explain.

5. Please explain why the United States stopped issuing ECGs under the SCGP program as of 1 October 2005.

6. On 23 January 2006, USDA invited public comment on "options to reform" SCGP. Those comments were due by 23 February 2006. What form will the results of USDA's reform inquiry take, and when will those results be released? When does USDA intend to re-commence issuance of guarantees under the SCGP program?

7. Please prepare a table showing correspondence between the so-called "scheduled" products listed in Table ES:1 of document G/AG/N/USA/53 and the list of products eligible for guarantees under the GSM 102 and the SCGP programs.

8. Please provide the calculation underlying the "subsidy rates for credit guarantee programs" stated on page 21 to the Notes to Financial Statements of the CCC for fiscal years 2004 and 2005 (available at http://www.usda.gov/oig/rptsauditsccc.htm). Please provide these calculations also for fiscal years 2002 and 2003.

9. Please provide the calculation underlying the "original subsidy rate" and "current reestimated rate" columns in Table 8 of the Federal Credit Supplement to the Fiscal Year 2007 Budget of the United State Government (available at http://www.whitehouse.gov/omb/budget/fy2007/), with respect to the CCC Export Loan Guarantee Programs.

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[4] *See* http://www.usda.gov/wps/portal/!ut/p/_s.7_0_A/7_0_1OB?contentidonly=true&contentid=2005/07/0242.xml.

[5] *See* http://www.usda.gov/oce/forum/2006%20Speeches/PDF%20speech%20docs/Goodloe2806.pdf.

10. In the original panel proceedings in WT/DS267, the United States provided, as Exhibit US-150, two memoranda, dated 8 April 2002 and 25 March 2003, titled "Annual Review of Fees for USDA Credit Programs". Please provide any memoranda or similar documents constituting annual reviews for subsequent years.

11. Please list and describe all criteria taken into account by CCC in setting the fee schedule for the GSM 102 and SCGP programs, and in determining the applicable fee for a guarantee for a particular transaction.

12. In determining the applicable fee for a GSM 102 or SCGP guarantee for a particular transaction, is the interest rate spread charged by the market to banks or borrowers in the foreign country involved examined, to identify changing market conditions? If the answer is in the affirmative, please provide documentary proof that demonstrates how this factor is taken into account.

13. What return does CCC require on capital employed, both across all of its programs and, more specifically, for the GSM 102 and SCGP programs?

14. Please indicate at what interval fee schedules for the GSM 102 and SCGP programs are reviewed. Please provide CCC regulations or procedures listing the elements to be taken into account during a review of the fee schedules.

15. Please provide data regarding the value of guaranteed transactions, by tenor and by country (rather than by CCC regional groupings), separately for GSM 102, GSM 103 and SCGP, by year for each of fiscal years 2000-2006.

16. For fiscal year 2006, please separate announced allocations for GSM 102 into individual country allocations, rather than CCC regional group allocations.

17. Please provide data regarding fees collected, by country (rather than by CCC regional groupings), separately for ECGs issued under GSM 102, GSM 103 and SCGP, by year for each of fiscal years 2000-2006.

18. For each country eligible for export credit guarantees through the GSM 102 and the SCGP programs, please provide the sovereign-risk rating and the private risk-rating established through the Interagency Country Risk Assessment System (ICRAS), as well as any ICRAS papers or analyses justifying those ratings.

19. Brazil understands that ICRAS has established eleven sovereign and nine nonsovereign risk categories for use by U.S. government agencies and programs providing cross-border loans, guarantees or insurance. Does CCC classify GSM-approved foreign banks, as well as foreign borrowers under the GSM 102 and SCGP programs, according to these same eleven sovereign and nine nonsovereign risk categories?

20. If the answer to the previous question is in the negative, please indicate the number of risk categories into which CCC classifies guarantees for the GSM 102 and SCGP programs, and explain: (i) how those risk categories are established; and (ii) how those risk categories correspond to the ICRAS categories.

21. Whether CCC uses the ICRAS risk categories or its own risk categories, please:

(a) provide a correspondence table and documentary support showing the correspondence between the CCC risk categories and the ratings (*e.g.*, BB, BBB, BBB-, etc.) in the Moody's or Standard and Poor's rating systems;

(b) for fiscal years 2000-2006, indicate the value of guaranteed transactions in each CCC risk category for GSM 102 guarantees issued in each of those years;

(c) for fiscal years 2000-2006, indicate the value of guaranteed transactions in each CCC risk category for SCGP guarantees issued in each of those years;

(d) for fiscal years 2005 and 2006, indicate the value of guaranteed transactions in each CCC risk category for the portfolio of GSM 102 guarantees outstanding on the last day of each fiscal year;

(e) for fiscal years 2005 and 2006, indicate the value of guaranteed transactions in each CCC risk category for the portfolio of SCGP guarantees outstanding on the last day of each fiscal year.

22. In each of fiscal years 2000-2006, please list the percentage of importers/purchasers in export transactions for which an SCGP guarantee is provided that are government-owned or -controlled, or quasi-government-owned or -controlled.

23. Please describe the profile of a typical importer/purchaser in export transactions for which an SCGP guarantee is provided, in terms of loan size, importer/purchaser's asset size, and importer/purchaser's credit rating.

24. Please describe how loss or default rates on SCGP guarantees vary for different importer/purchaser profiles (again, in terms of loan size, importer/purchaser's asset size, and importer/purchaser's credit rating).

25. For the cohort of SCGP guarantees issued in each of fiscal years 2000-2006, please provide a chart that divides the cohort according to the value of the transactions guaranteed. Please use increments of $1000.

26. For the cohort of SCGP guarantees issued in each of fiscal years 2000-2006, please provide a chart that divides the cohort according to the credit rating of the borrower/purchaser.

27. For the cohort of SCGP guarantees issued in each of fiscal years 2000-2006, please provide a chart that divides the cohort according to the value of the transactions guaranteed, and, further, indicates loss or default rates for each increment of transaction value.

28. For the cohort of SCGP guarantees issued in each of fiscal years 2000-2006, please provide a chart that divides the cohort according to the credit rating of the borrower/purchaser, and, further, indicates loss or default rates for each category of credit rating.

29. For the cohort of GSM 102 guarantees issued in each of fiscal years 2000-2006, please provide a chart that divides the cohort according to the value of the transactions guaranteed. Please use increments of $1000.

30. For the cohort of GSM 102 guarantees issued in each of fiscal years 2000-2006, please provide charts that divide the cohort according to the credit rating of the foreign bank, and of the borrower/purchaser.

31. For the cohort of GSM 102 guarantees issued in each of fiscal years 2000-2006, please provide a chart that divides the cohort according to the value of the transactions guaranteed, and, further, indicates loss or default rates for each increment of transaction value.

32. For the cohort of GSM 102 guarantees issued in each of fiscal years 2000-2006, please provide charts that divide the cohort according to the credit rating of the foreign bank, and of the borrower/purchaser, and, further, indicates loss or default rates for each category of credit rating.

33. Please provide data and documentary support addressing default rates for the GSM 102 and SCGP programs (both separately and together) for each fiscal year during the period 2000-2006.

34. How does CCC arrive at the default and loss estimates presumably used to determine fees for GSM 102 and SCGP guarantees?

35. For each country eligible for export credit guarantees through the GSM 102 and the SCGP programs, please provide the Office of Management and Budget's (OMB) default estimate. (OMB's default estimate methodology is discussed on page 79 of the "Analytical Perspectives" document associated with the U.S. 2007 budget, available at http://www.whitehouse.gov/omb/budget/fy2007/).

36. How does the OMB default estimate affect the fee schedule for the GSM 102 and SCGP programs? What, if any, discretion does CCC enjoy to depart from the OMB default estimate in setting fees for the GSM 102 and SCGP programs?

37. How does CCC fund accumulated losses?

38. What was the total amount of outstanding principal and interest guaranteed through GSM 102, GSM 103 and SCGP on 1 July 2005? Please provide data separately for each of the three programs. With respect to this data:

(a) What proportion of the outstanding principal and interest was associated with exports of unscheduled products, and what proportion was associated with exports of scheduled products?

(b) Of the proportion associated with scheduled products, what proportion was associated with exports of rice?

39. Page 30 of the "Notes to Financial Statements" included with the CCC's Financial Statements for Fiscal Years 2005 and 2004 (available at http://www.usda.gov/oig/rptsauditsccc.htm) lists the value of guaranteed transactions outstanding on 1 September 2005, divided by maturity date. Please provide a similar chart with data as of 1 July 2005.

40. Does the CCC require that a party (*e.g.*, the exporter) to an export transaction for which an SCGP guarantee is requested seek and provide to CCC credit references for the importer/purchaser? Does the CCC itself seek such credit references? If answered in the affirmative, please provide the relevant regulations or procedures setting out this requirement.

41. Does CCC require information regarding the credit rating of an importer/purchaser in an export transaction for which and SCGP guarantee is requested? If answered in the affirmative, please provide the relevant regulations or procedures setting out this requirement.

42. CCC maintains a list of foreign bank obligors approved for participation in the GSM 102 program. The list is available at http://www.fas.usda.gov/excredits/foreignbanks.html. Does CCC inquire into the credit rating for these banks? If so, please provide the credit rating for the banks currently approved.

43. Are there statutory or regulatory limits on the level of exposure (in terms of the value of transactions, or any other variable) CCC can maintain, under the SCGP program, with respect to any

given importer? If answered in the affirmative, please provide regulations or procedures setting out the limits.

44. Are importers included on the default lists of the American Cotton Exporters Association (ACEA) or the World Cotton Exporters Association (WCEA) allowed to participate in transactions involving GSM 102 or SCGP guarantees?[6]

45. Please provide a copy of any agreement governing the relationship between the U.S. government and CoBank, with respect to CoBank's role as a lender under the GSM 102 program.

46. ExpectMore.gov has undertaken an assessment of the "Agricultural Export Credit Guarantee Programs" subject to these consultations. The assessment (program code 10002020), is available at http://www.whitehouse.gov/omb/expectmore/detail.10002020.2005.html. Please provide the following documents, identified as "Evidence" in the assessment (each of which is highlighted in the attached copy of the assessment):

- FAS Credit Guarantee Program Analysis;
- FAS GSM to Exports Powerpoint;
- FAS Portfolio Analysis (annual) (please provide for FY 1999 to the present, or if maintained on a calendar or marketing year basis, then for calendar or marketing years 1999 to the present);
- Contingent Liability by Country Risk Grade Powerpoint;
- FAS Decision Memo, 4/12/04 department wide meeting with OMB
- CCC Exposure Report (monthly) (please provide for all months from FY 1999 to the present);
- FAS Risk Assessment Handbook;
- Geographic and Commodity Analysis (quarterly) (please provide for all quarters from FY 1999 to the present);
- Commercial Export Credit Report (quarterly) (please provide for all quarters from FY 1999 to the present).

[Annex 1 and Annex 2 to this document omitted.]

[6] These lists are maintained at http://www.acsa-cotton.org/Default_Lists/ACEA_Default_List/body_acea_default_list.asp (for ACEA) and http://www.acsa-cotton.org/Default_Lists/WCEA_Default_List/body_wcea_default_list.asp (for WCEA).

ANNEX D-2

RESPONSES OF BRAZIL TO THE PANEL'S QUESTIONS ON THE DSU ARTICLE 13 ISSUE

(19 January 2007)

Question 1 (to Brazil)

Does Brazil deem that the questions posed in Part B[1] of Annex 1 of its request submitted on 1 November 2005 ("1 November request" hereafter) are now unnecessary?

1. Brazil continues to believe that the information, documents and data requested in Part B of Annex 1 of its request submitted on 1 November 2005 ("1 November Request") will assist the compliance Panel in making "an objective assessment of the matter before it," within the meaning of Article 11 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU").

2. Brazil notes that the documents requested in questions 17-23 of Annex 1 to Brazil's 1 November Request were cited by the U.S. Department of Agriculture's Foreign Agriculture Service in a self-assessment of the export credit guarantee ("ECG") programs. This self-assessment was provided to the compliance Panel as Exhibit Bra-588.

3. In previous discussions, the United States noted uncertainty regarding the definition of the term "default rate," as used in questions 13 and 14 of Annex 1 to Brazil's 1 November Request. To clarify, Brazil uses the term as it is used by the Commodity Credit Corporation ("CCC") in its financial statements. Specifically, on page 28 of the Notes to the CCC's fiscal year 2006 and 2005 financial statements, provided to the compliance Panel as Exhibit Bra-585, CCC details "defaults" for the ECG programs, phrased in percentage terms (and therefore as *rates* of default).[2]

Question 2 (to Brazil)

Is Brazil asking the United States to respond to all of the questions posed in Part A of its 1 November request?

4. Brazil asks that the compliance Panel request the United States to provide data responsive to all questions in Part A of Brazil's 1 November Request. The information provided by the United States in the table in Section VI.A.(c) of its First Written Submission[3] demonstrates that the United States has already collected and compiled the data necessary to respond to most, if not all, of Part A of Annex I of Brazil's 1 November Request.

5. Brazil recalls that its 1 November Request, like the request by the original panel, distinguishes between three categories of U.S. upland cotton farms: A, B and C.

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[1] Concerning Export Guarantee Programs.

[2] These rates are only offered in the aggregate, and not for individual ECG programs or as related to the credit ratings of obligors; Brazil has asked for further detail in its questions.

[3] U.S. First Written Submission, para. 224.

6. With respect to Category A farms[4], *i.e.*, upland cotton farms that "underplant" their base acreage, Brazil notes that the table in Section VI.A.(c) of the U.S. First Written Submission[5] provides incomplete information. While the United States provides information responsive to the question: "What was the total of their upland cotton planted acreage?"[6], the United States does not provide information responsive to the following question: "What was the total of their upland cotton base acreage?" Further, the United States provides no information for farms that have upland cotton bases acres but no planted acres (Category A-1 farms[7]). These omissions make it impossible for Brazil to update Tables A-1 and A-3 of the original panel's report.[8] Finally, the United States provides no information on the actual *number of farms* that fall into these categories.

7. With respect to Category B farms, *i.e.*, farms that "overplant" their upland cotton base acreage[9], and with respect to Category C farms, *i.e.*, upland cotton farms that have no upland cotton base acreage[10], Brazil notes that the United States also provides information that is partially responsive to the questions proposed by Brazil. In particular, the table in Section VI.A.(c) of the U.S. First Written Submission[11] provides information on the total number of upland cotton base and upland cotton planted acres on these farms. This information, along with the limited information provided with respect to Category A farms, enables Brazil to update Tables A-2, A-4 and A-5 of the original panel's report.[12] However, the United States does not provide information on the base and planted acreage of other covered commodities on these farms. This makes it impossible for Brazil to update Table A-6 of the original panel's report.[13] The United States also provides no information on the actual *number of farms* in these categories.

8. Finally, the United States does not provide information on direct and counter-cyclical payment units for each program crop and each category of farm.

9. In sum, the U.S. First Written Submission answered some of the questions in Part A of Annex I to Brazil's 1 November Request. This partial response demonstrates that the United States has collected and compiled most, if not all, of the data necessary to fully respond to Brazil's 1 November Request. Brazil, therefore, requests that the compliance Panel ask the United States to fully respond to Brazil's 1 November Request.

10. Specifically, Brazil identifies the questions that it considers remain unanswered based on the data submitted by the United States as part of its First Written Submission. For each of these questions, Brazil asks that the compliance Panel request the United States to provide annual data covering the period MY 2002-2005:

(a) How many Category A farms were there in the period? How many base acres were on Category A farms?

(b) How many Category A-1 farms were there in the period? How many base acres were on Category A-1 farms?

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[4] *See* Part A of Question 1(A) of Annex I of Brazil's 1 November 2006 Request.
[5] U.S. First Written Submission, para. 224.
[6] *See* Row 1 of the United States table at paragraph 224 of the U.S. First Written Submission.
[7] *See* Part A, Question 1(A)(1) of Annex I of Brazil's 1 November 2006 Request.
[8] *See* Panel Report, *U.S. – Upland Cotton*, paras. 7.636 and 7.639.
[9] *See* Part A, Question 1(B) of Annex I of Brazil's 1 November 2006 Request.
[10] *See* Part A, Question 1(C) of Annex I of Brazil's 1 November 2006 Request.
[11] U.S. First Written Submission, para. 224.
[12] *See* Panel Report, *U.S. – Upland Cotton*, paras. 7.636, 7.639 and 7.641.
[13] *See* Panel Report, *U.S. – Upland Cotton*, para. 7.642.

(c) How many Category B farms had equal numbers of acres planted to all covered commodities and base acres for all covered commodities? Brazil refers to these as "Category B-1" farms. What was the total of the base acreage of Category B-1 farms for each covered commodity, including upland cotton? What was the total of the planted acreage of Category B-1 farms for each covered commodity, including upland cotton?

(d) How many Category B farms had fewer acres planted to all covered commodities than base acres for all covered commodities? Brazil refers to these as "Category B-2" farms. How much was the total acreage of Category B-2 farms planted to all covered commodities less than their base acreage for all covered commodities? What was the total of the base acreage of Category B-2 farms for each covered commodity, including upland cotton? What was the total of the planted acreage of Category B-2 farms for each covered commodity, including upland cotton?

(e) How many Category B farms had more acres planted to all covered commodities than base acres for all covered commodities? Brazil refers to these as "Category B-3" farms. How much did the total acreage of Category B-3 farms planted to all covered commodities exceed their base acreage for all covered commodities? What was the total of the base acreage of Category B-3 farms for each covered commodity, including upland cotton? What was the total of the planted acreage of Category B-3 farms for each covered commodity, including upland cotton?

(f) How many Category C farms were there in the period? What was the total of the base acreage of Category C farms for each covered commodity? What was the total of the planted acreage of Category C farms for each covered commodity, including upland cotton?

(g) What were the average counter-cyclical payment yields for each program crop on each category of farm?

ANNEX D-3

RESPONSES OF THE UNITED STATES TO THE PANEL'S QUESTIONS ON THE DSU ARTICLE 13 ISSUE

(19 January 2007)

The United States is in receipt of the Panel's communication dated January 17, 2007, in which it poses questions to the parties regarding Brazil's November 1, 2006, request that the Panel collect more than 35 different data items or documents pursuant to Article 13 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU"). My authorities have instructed me to provide the following responses:

Question 3 (to the United States)

If the United States is of the view that the Panel should not pose to the United States any or all of the questions in Part A of Brazil's 1 November request, please cite the reasons for that view.

Question 4 (to the United States)

If the United States is of the view that the United States cannot respond to any or all of the questions (or any part thereof) in Part A of Brazil's 1 November request, please explain that view, bearing in mind the fact that the United States did provide the data to the original Panel.

1. The Panel notes in its communication that, in its rebuttal submission, Brazil reiterated its request that the Panel collect certain data and documents from the United States pursuant to Article 13.1 of the DSU.[1] Brazil complains in that submission that the Panel does not have before it certain data collected by the original panel at Brazil's urging regarding farms that hold base acres under the counter-cyclical program and those farms' planted acres for cotton and other program crops.[2] However, Brazil's assertion is factually incorrect as the United States submitted the relevant data as an exhibit to its first written submission.

2. In Exhibit US-64, the United States submitted precisely the same data in precisely the same format as that submitted in response to the original panel's Article 13 request.[3] Moreover, the United States explained in Annex I to its first written submission how these data are relevant to the claims and arguments at hand. Specifically, the data fatally undermine the analysis of Brazil regarding the effects of the counter-cyclical payment program.[4] Brazil has attempted to attribute an entirely exaggerated effect to the counter-cyclical program by speculating, *inter alia*, that restrictions on payments when fruits and vegetables are planted on acreage in excess of a farm's non-base acres serve to funnel planting decisions towards upland cotton because fruits and vegetables are allegedly "the most relevant alternative in some major cotton areas."[5] However, the empirical data requested by

[1] January 17, 2007 Communication from the Panel.
[2] *See* Brazil Rebuttal Submission, para. 164.
[3] *See* Response of the United States to the Panel's February 3, 2004, Data Request, As Clarified on February 16, 2004 (providing 8 data files via CD-ROM) (March 3, 2004).
[4] U.S. First Written Submission, Annex I, paras. 36-37.
[5] Brazil First Written Submission, Annex I, para. 63.

Brazil and presented in Exhibit US-64 demonstrate that Brazil's argument is pure speculation and contradicted by the facts.[6]

3. The United States also notes that the Panel should reject Brazil's argument for how the data in Exhibit US-64 should be used; namely, to allocate counter-cyclical payments for both cotton base acres and non-cotton base acres to upland cotton production using its self-titled "Brazil methodology."[7] This argument misrepresents the panel and Appellate Body's analyses in the original proceeding and ignores the resulting recommendations and rulings of the DSB. First, this "Brazil methodology" was *not* applied in the context of the panel's assessment of significant price suppression, as Brazil has implied, and therefore neither the Panel's finding of serious prejudice, nor the resulting DSB recommendations and rulings, extended to counter-cyclical payments for non-cotton base acres.[8] Rather, as is clear from a review of Brazil's citations[9], it was only addressed in the context of the original panel's analysis of "support to a specific commodity" under Article 13(b) of the *Agreement on Agriculture* (the "Peace Clause" analysis). And, even in that context it was specifically *rejected*. In fact, while Brazil touts the original panel's characterization of this methodology as "appropriate,"[10] that panel did not rely on the methodology in its Peace Clause analysis.[11] Moreover, Brazil fails to mention that when it raised the methodology on appeal, the Appellate Body specifically indicated that the methodology was unacceptable:

> [W]e see little in the Panel's finding or on the record that would allow us to discern a link between the support-conferring measures with respect to non-cotton historical base acres and current production of upland cotton. *We do not, therefore, accept the methodology submitted by Brazil* that included, in the Article 13(b)(ii) calculation, payments with respect to both cotton and non-cotton base acres flowing to current production of upland cotton.[12]

4. Thus, because "support-conferring measures with respect to non-cotton historical base acres" were *not* included in the support found to exceed the limitation in the Peace Clause proviso, such measures were exempt, by virtue of the Peace Clause, from actions, including Brazil's serious prejudice claims. Therefore, there could have been no, and there were no, DSB recommendations and

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[6] Specifically, the ratio of upland cotton base acres to planted acres on such farms was low (for example, only 32.7 percent in California), showing that there is no basis for the funneling effect claimed by Brazil. Further, only about *one third* of the acres planted to cotton in the historical "base" period were still planted to cotton in MY 2005. Moreover, in those areas in which fruits and vegetables are a viable alternative to cotton, substantial acreage was planted to fruits and vegetables on farms with upland cotton base acreage (for example, 600,000 acres in California and more than 1 million acres nationwide). This too demonstrates that farmers do not feel compelled to plant cotton rather than fruits and vegetables on these farms. As the United States will explain in its forthcoming rebuttal submission, Brazil has no answer to these U.S. arguments.

[7] This is the methodology under which Brazil attempts to further exaggerate the amount of counter-cyclical payments by including payments made in respect of base acres for other programs crops simply because they were made on farms on which the number of acres planted to cotton exceeded the number of upland cotton base acres held by the farm operator. Brazil Rebuttal Submission, para. 171.

[8] *See, e.g.*, Brazil's November 1, 2006 request, paras. 9-13. Indeed, it is surprising that Brazil makes this argument given that it vehemently opposed *any* precise calculation of the subsidy in the context of the significant price suppression analysis (arguing that it was sufficient for the original panel to simply to find that the payments under the Step 2, marketing loan, and counter-cyclical payment programs were allegedly, respectively, "very large"). *See, e.g., United States – Upland Cotton (AB)*, paras. 98-99.

[9] Most of Brazil's citations in its November 1 request are to the following paragraphs: 7.608-7.633 and 7.641-7.647. These refer to the section of the original panel report entitled "Conclusion regarding Article 13(b)" and to an "Attachment to Section VII:D" (which is itself entitled "Domestic Support Measures and Article 13 of the *Agreement on Agriculture*").

[10] *See, e.g.*, Brazil Rebuttal Submission, para. 172.

[11] *United States – Upland Cotton (Panel)*, para. 7.580.

[12] *United States – Upland Cotton (AB)*, para. 380.

rulings with respect to such measures, and counter-cyclical payments for non-cotton base acres are not "measures taken to comply" within the meaning of DSU Article 21.5.

5. In sum, Brazil's renewed request in its rebuttal submission that the Panel collect the data items listed in Part A of Annex 1 of Brazil's November 1 request is moot since the United States has already provided the data for the period relevant to Brazil's present serious prejudice claims. Moreover, Brazil's arguments about the relevance of this information are incorrect and misleading; to the extent they are relevant, the data support the U.S. view. In light of the foregoing, the United States respectfully requests the Panel to reject the renewed request.

6. As the Panel has invited each of the parties to comment on any of the questions posed to the other party, the United States also provides the following brief comment relating to Question 1 directed to Brazil:

Question 1 (to Brazil)

Does Brazil deem that the questions posed in Part B of Annex 1 of its request submitted on 1 November 2005 ("1 November request" hereafter) are now unnecessary?

7. To date, Brazil has failed to provide *any* reason in its November 1 request, its first submission, or its rebuttal submission why the Panel should collect the more than 25 items listed in Part B of Annex 1 of its November 1 request. Nor has Brazil provided the type of item-by-item explanation that is needed for *the Panel* to determine whether these items are indeed "necessary and appropriate" within the meaning of Article 13 of the DSU for the Panel's objective assessment of the evidence and arguments submitted by the parties. Under these circumstances, there is no basis to grant Brazil's request.

ANNEX D-4

COMMENTS OF BRAZIL ON THE ORAL STATEMENTS OF THE UNITED STATES AT THE MEETING WITH THE PANEL

(9 March 2007)

TABLE OF CONTENTS

LIST OF FIGURES AND TABLES

LIST OF ABBREVIATIONS

DSU	Understanding on Rules and Procedures Governing the Settlement of Disputes
FAPRI	Food and Agricultural Policy Research Institute
FSRI Act	Farm Security and Rural Investment Act of 2002
ICAC	International Cotton Advisory Committee
MY	Marketing Year
SCM Agreement	*Agreement on Subsidies and Countervailing Measures*
U.S.	United States
USDA	U.S. Department of Agriculture
WTO	World Trade Organization

LIST OF EXHIBITS

U.S. Export Sales Data, accessed at www.fas.usda.gov/export-sales/h1404.htm	Exhibit Bra-663
Monthly Export Sales	Exhibit Bra-664
Analysis of Planting Decisions Based on Expected Returns and Cash Costs	Exhibit Bra-665
Actual Costs and Returns Analysis Based on Cash Costs	Exhibit Bra-666
Expected Costs and Returns Using Variable Costs	Exhibit Bra-667
Actual Costs and Returns Using Variable Costs	Exhibit Bra-668
"Adoption of Genetically Engineered Crops in the U.S.: Cotton Varieties," Economic Research Service, U.S. Department of Agriculture, accessed March 2007 at http://www.ers.usda.gov/data/biotechcrops/ExtentofAdoptionTable2.htm	Exhibit Bra-669

TABLE OF CASES

Short Title	Full Case Title and Citation
Brazil – Aircraft (21.5)	Appellate Body Report, *Brazil – Export Financing Program for Aircraft – Recourse by Canada to Article 21.5 of the DSU*, WT/DS46/AB/RW, adopted 4 August 2000, DSR 2000:VIII, 4067.
U.S. – FSC (21.5)	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW, adopted 29 January 2002, DSR 2002:I, 55.
U.S. – FSC (21.5 II)	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Second Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW2, adopted 14 March 2006.
U.S. – Softwood Lumber IV	Appellate Body Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R, adopted 17 February 2004, DSR 2004:II, 571.

1. INTRODUCTION

1. Brazil thanks the compliance Panel for the opportunity to comment on the United States' Opening and Closing Statement at the Panel Meeting. In this submission, Brazil comments on selected issues and arguments raised by the United States. Brazil also refers the compliance Panel to its own Closing Statement at the Panel Meeting, in which Brazil responded to the majority of new U.S. arguments.

2. Specifically, in its Closing Statement, Brazil made, *inter alia*, the following points in response to U.S. adverse effects-related arguments:

- Mandatory and price-contingent marketing loan and counter-cyclical subsidies granted subsequent to the original panel's reference period are properly before this compliance Panel.[1]

- Brazil's argument that there is a rapid transmission of prices in an integrated world market is consistent with the fact that farmers outside the United States react more slowly to higher prices from the elimination of U.S. subsidies.[2]

- The fact that the average acre planted to upland cotton covered its production costs with market returns in MY 2003 was an aberration.[3]

- Brazil has demonstrated that the world market price-suppressing effects from marketing loan and counter-cyclical subsidies are "significant."[4]

3. Additionally, in its Closing Statement, Brazil made the following points in response to the U.S. export credit guarantee-related ("ECG") arguments:

- The amended GSM 102 program does not meet its long-term costs and losses, under item (j) of the Illustrative List. The U.S. government continues, every year, to project that GSM 102 ECGs issued in that year will result in losses.[5]

- Even if the GSM 102 program meets its long-term operating costs and losses, within the meaning of item (j), this does not, under the proper interpretation of footnote 5 to the SCM Agreement, "demonstrate[] dispositively" that GSM 102 ECGs are not export subsidies.[6]

- Even if the GSM 102 program meets its long-term operating costs and losses, the United States has failed to achieve "full withdrawal" of the prohibited subsidy, instead merely replacing it with another prohibited subsidy. Specifically, under the amended fee schedule, GSM 102 ECGs are export-contingent contributions that confer "benefits".[7]

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[1] Brazil's Closing Statement, paras. 2-4.
[2] Brazil's Closing Statement, paras. 5-8.
[3] Brazil's Closing Statement, paras. 15-16.
[4] Brazil's Closing Statement, paras. 17-20.
[5] Brazil's Closing Statement, paras. 21-22.
[6] Brazil's Closing Statement, para. 24, *quoting* U.S. Oral Statement, heading III.A.1.
[7] Brazil's Closing Statement, paras. 25-27, *quoting* Appellate Body Report, *U.S. – FSC (21.5 II)*, para. 83.

- Article 14(c) of the SCM Agreement sets forth only "guidelines" that the Appellate Body, at the United States' urging, has concluded must not be followed rigidly, even in countervailing measure disputes to which the provision expressly applies.[8]

- By continuing to pay claims on certain ECGs outstanding on 1 July 2005, the United States has failed to "withdraw the subsidy", under the interpretation of that phrase made by the Appellate Body.[9]

4. Brazil will not revisit these points, but will instead address a number of additional adverse effects-related issues raised in the United States' Opening and Closing Statements. In this submission, Brazil does not offer any additional comments on ECG-related issues raised in the United States' Opening and Closing Statements.

2. LOWER U.S. EXPORTS IN MY 2006 ARE DRIVEN BY LOWER WORLD DEMAND, NOT THE ELIMINATION OF THE STEP 2 PROGRAM

5. The United States continues to argue that the elimination of the Step 2 program caused the decrease in U.S. upland cotton exports in MY 2006.[10] As explained in Brazil's Closing Statement, this is inaccurate.[11]

6. The United States has provided weekly February export data to show that the repeal of the Step 2 program has resulted in a decline in exports. By comparing MY 2006 to MY 2005, the United States claims that "U.S. exports are *down 30 per cent*".[12] However, the United States fails to mention that exports surged prior to the repeal of the Step 2 program. Data shows that prior to the elimination of Step 2 subsidies, sales were at their second highest level for the MY 2002-2007 period.[13] Considering the average of the two months prior to the repeal of Step 2 subsidies (June-July 2006) and the two subsequent months (August-September 2006), reveals that exports fell by 85 per cent. In other words, they were 7 times less.[14] Brazil also notes that during the two months prior to the elimination of Step 2 subsidies, U.S. exports were close to double their average over the previous five- marketing years (MY 2000-2004).[15] One consequence of these massive sales in MY 2005 is a subsequent decline in exports in MY 2006. This is consistent with the attempt by rational exporters to cash in the last available Step 2 payments.

7. During the first weeks of calendar year 2007, *i.e.*, half-way through MY 2006, data on U.S. exports continues to show lower sales. The United States attributes this to the elimination of Step 2. A close analysis of world trade however provides a different explanation. In fact, all major cotton exporters, with the exception of India, have seen their exports decline in MY 2006.[16] The primary reason for this decline is weak international demand. As Brazil has repeatedly shown by providing market reports, China, the biggest importer, is using up "a large supply of cotton imported prior to the

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[8] Brazil's Closing Statement, paras. 28-29, *citing* Appellate Body Report, *U.S. – Softwood Lumber IV*, para. 92.

[9] Brazil's Closing Statement, para. 30, *citing* Appellate Body Report, *U.S. – FSC (21.5)*, paras. 2, 223-231, and Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 45.

[10] Brazil notes that the United States fails to provide the source for some of its data (*See, e.g.*, U.S. Oral Statement, para. 11) or does not provide the link to its data (*See, e.g.*, U.S. Oral Statement, para. 10.).

[11] Brazil's Closing Statement, para. 11.

[12] U.S. Oral Statement, para. 10.

[13] Exhibit Bra-663 (U.S. Export Sales Data, accessed at www.fas.usda.gov/export-sales/h1404.htm).

[14] Exhibit Bra-664 (Monthly Export Sales).

[15] Exhibit Bra-664 (Monthly Export Sales).

[16] Exhibit Bra-652 (International Cotton Advisory Committee Review, Volume 60, Number 3 January-February 2007, accessed February 2007, p. 4).

expiration of the Step 2 program."[17] Increasing Indian exports have added to export declines in the United States and other exporting countries.[18] These undisputed facts largely explain the decline in the U.S. share of Chinese imports and in the U.S. share of world exports.[19]

8. Moreover, the reduction in U.S. exports must be viewed in perspective. Brazil notes that USDA (and ICAC) currently project U.S. exports in MY 2006 to be the *second highest in history* and comparable to MY 2004 levels.[20] In addition, projections for MY 2007 and 2008 show an expected annual increase of almost 10 percent compared to MY 2006 and 2007, respectively.[21]

9. Thus, the present decline in U.S. share of exports is not a result of Step 2 elimination but a result of overall declining world trade.

3. BRAZIL HAS NOT CHANGED ITS POSITION REGARDING THE CAUSE OF SIGNIFICANT PRICE SUPPRESSION

10. The United States claims that Brazil has shifted position from asserting that exports cause price suppression, to asserting that stocks and production cause price suppression. Moreover, the United States asserts that it is "too late … to be altering fundamental factors" and that Brazil submits "no evidence or argument to substantiate its new assertion."[22] These U.S. claims are false.

11. Brazil has not changed its position. Production, stocks and exports are interlinked – all constitute supply; any supply not consumed domestically must eventually be exported.[23] Indeed, this is a question of basic economics. Whether U.S. supply – generated by U.S. subsidies – ends up temporarily in a warehouse, or is exported immediately, this excess supply suppresses world market prices. In his Oral Statement during the Panel Meeting, Andrew Macdonald confirmed this relationship.[24]

12. In its Oral Statement, the United States noted that domestic U.S. mill use for MY 2006 is decreasing.[25] This lack of domestic demand for U.S. supply also contributes to the accumulation of stocks of subsidy-generated U.S. upland cotton that will eventually be exported. Again, whether U.S. supply resulting from subsidized production is exported immediately, or ends up temporarily as stocks and is exported later, it affects, and in fact suppresses, world market prices for upland cotton.

4. AN ANALYSIS OF UPLAND COTTON VARIABLE COSTS AND RETURNS SUPPORTS BRAZIL'S SERIOUS PREJUDICE CLAIMS

13. Next, Brazil addresses U.S. arguments regarding the "expected" and "actual" total costs and return charts presented in Brazil's Oral Statement. These charts visually illustrate two effects of upland cotton marketing loan and counter-cyclical subsidies.[26] First, the charts show that marketing loan and counter-cyclical subsidies are essential for upland cotton farmers to be able to cover their

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[17] Exhibit Bra-662 (Elton Robinson, "High certificated cotton stocks slow trade, weigh on prices," Delta Farm Press, 1 December 2006, accessed February 2007 at http://deltafarmpress.com/mag/farming_high_certificated_cotton/).

[18] Exhibit Bra-652 (International Cotton Advisory Committee Review, Volume 60, Number 3 January-February 2007, accessed February 2007, p. 4).

[19] U.S. Oral Statement, paras. 10-11.

[20] Exhibit Bra-651 (Cotton and Wool Outlook, USDA, 12 February 2007, p. 4, accessed February 2007 at http://usda.mannlib.cornell.edu/usda/current/CWS/CWS-02-12-2007.pdf).

[21] Exhibit Bra-635 (2002-2007 USDA Agricultural Baseline Projections, p. 46).

[22] U.S. Closing Statement, para. 15.

[23] Brazil's Closing Statement, paras. 9-14.

[24] *See* Brazil's Oral Statement, paras. 147, 160-162.

[25] U.S. Oral Statement, para. 11.

[26] Brazil's Oral Statement, paras. 63-78.

costs of production and stay in the business of growing upland cotton. Market revenue by itself is almost never sufficient, nor is it expected to be sufficient, to cover *total* costs. Further, expected and actual market revenue is below or just above average *variable* costs in a number of years, suggesting that many upland cotton farmers would exit cotton faming without marketing loan and counter-cyclical subsidies even in the short term. Similar evidence on the gap between U.S. upland cotton producers production costs and market returns has been presented in Brazil's First Written Submission[27], Rebuttal Submission[28] and Oral Statement.[29]

14. Second, the charts in Brazil's Oral Statement show that upland cotton farmers would exit upland cotton production by switching to the production of alternative crops but for the effect of marketing loan and counter-cyclical subsidies. Absent those subsidies, expected returns from growing corn or soybeans in almost every year make it more attractive to grow one of these alternative crops. This evidence responds to U.S. criticisms that Brail has not properly examined the relative attractiveness of competing crops at the time of planting.[30]

15. In its Oral Statement, the United States asserted that variable costs and market returns are the determinative factors driving farmers' year-to-year planting decisions.[31] Yet, during the second day of the Panel Meeting and in its Closing Statement, the United States admitted that certain fixed costs, including those that are "cash costs,"[32] are also pertinent to planting decisions.[33] Indeed, the second U.S. chart in the "U.S. Exhibit of February, 28 2007," entitled "Costs of producing cotton," includes variable and fixed costs that constitute cash costs. It excludes land, own-labour and capital recovery costs. However, these non-cash costs[34] account for almost 30 percent of the total cost of producing cotton.[35]

16. Brazil also notes that the first chart in the "U.S. Exhibit of February, 28 2007" is based on *actual* costs and *actual* market returns as realized in marketing year 2005. Brazil is puzzled that the United States presents a chart of *actual* returns minus cash costs, when, in the words of the United States, a farmer "cannot rewind time and make different production decisions based on how things actually turn out."[36] In other words, it is costs and *expected* returns at the time of planting that provide one useful means to assess the impact of marketing loan and counter-cyclical subsidies. This is the approach that Brazil has followed in figures 1-4 of its Oral Statement,

17. In any event, farmers can only survive by seeking to maximize their market and subsidy returns over *total* costs, including cash and imputed costs, when making planting decisions. Nevertheless, comparing total costs, variable costs or even cash costs to expected market returns leads

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[27] Section 7.11 of Brazil's First Written Submission, paras. 156-164.

[28] Section 2.3.6 of Brazil's Rebuttal Submission, paras. 245-289.

[29] Section 2.4 of Brazil's Oral Statement, paras. 54-91.

[30] *See* U.S. First Written Submission para. 255. *See also* U.S. Rebuttal Submission, paras. 269, 275, 300-301.

[31] U.S. Oral Statement, paras. 12 and 73.

[32] According to *The Commodity Costs and Returns Estimation Handbook* "cash costs are costs that require a cash payment at the time the transaction occurs or during a specified reported period such as a week or month." *See* Exhibit Bra-649 ("Conceptual Issues in Cost and Return Estimates," Chapter 2 of Commodity Costs and Returns Estimation Handbook, a report of the AAEA Task Force on Commodity Costs and Returns).

[33] *See* U.S. Exhibit of February 28, 2007. In this exhibit, the United States compares cash costs and actual market returns of growing upland cotton, corn and soybeans in MY 2005. According to the United States, cash costs include operating costs, hired labour, taxes, insurance and general overhead. *See also* U.S. Closing Statement, para. 17.

[34] Brazil notes that land is only a non-cash cost to the extent it is owned by the farm operator. Rented land is a cash cost.

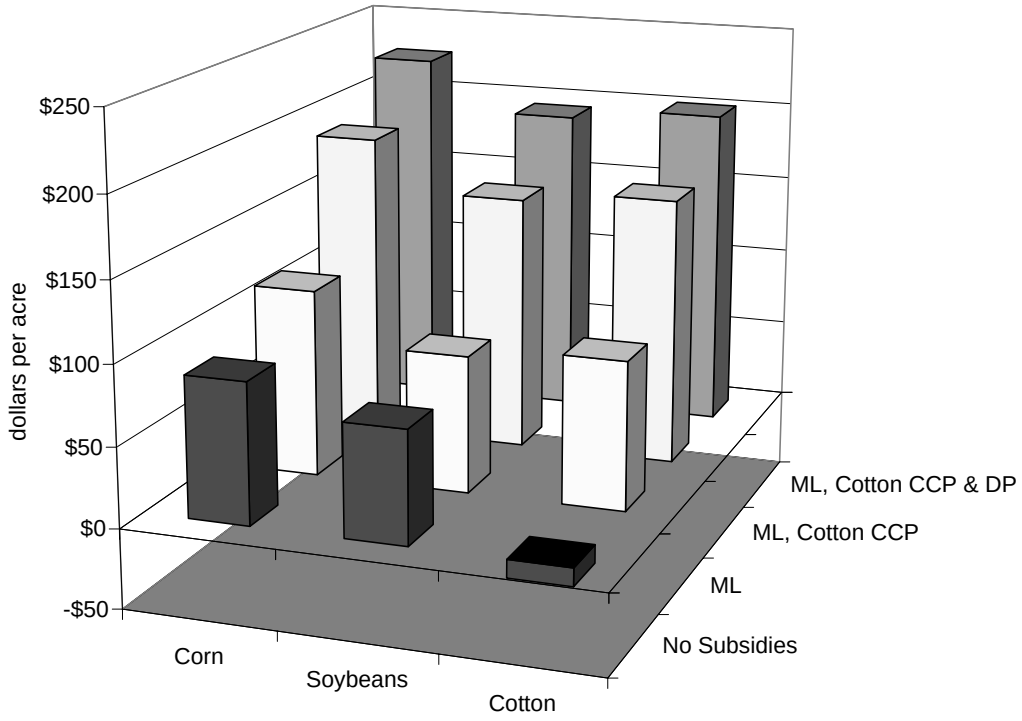
[35] Exhibit Bra-648 (Actual Costs and Returns Analysis).

[36] U.S. Oral Statement, paras. 4 and 65.

to the same basic conclusion: planting upland cotton without marketing loan and counter-cyclical payments would be economically irrational.

18. This irrationality is seen even when examining "cash costs," as identified by the United States in the U.S. Exhibit presented on 28 February 2007, compared to *expected* as well as *actual* revenue. Based on the relevant USDA and FAPRI data found in the attached exhibits, Figures 7 through 12, below, are based on *cash* costs, but conceptually mirror figures 1 through 6, respectively, of Brazil's Oral Statement, which were based on *total* cost.

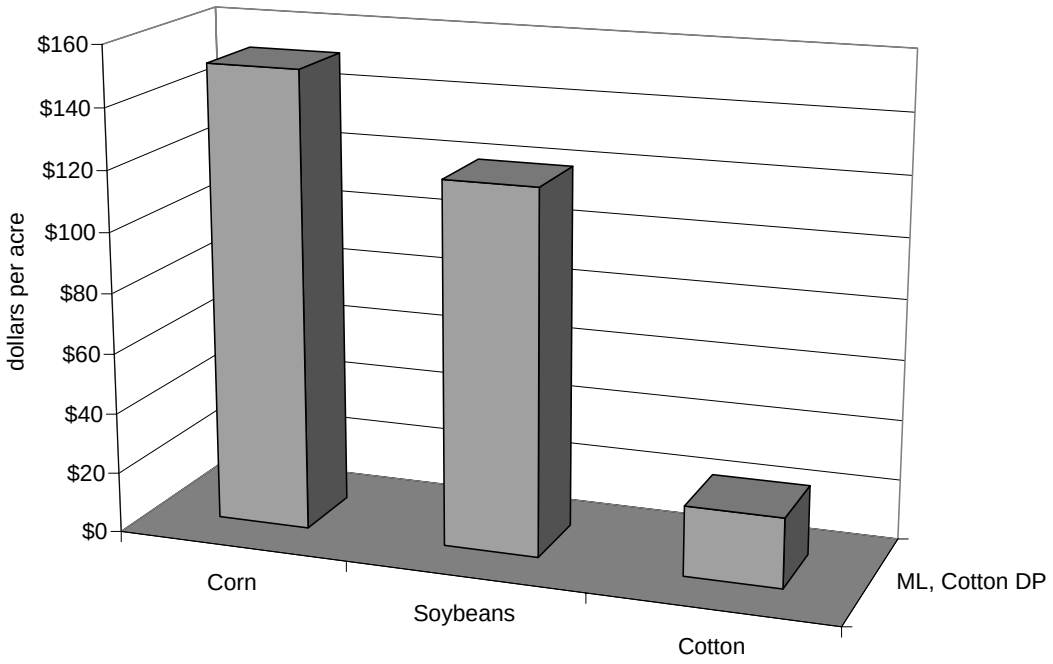
Figure 7 – <u>Expected Returns</u> in Excess of the <u>Cash Costs</u> of Growing Cotton, Corn or Soybeans on a Base Acre of Cotton in MY 2005[37]



19. Figure 7 demonstrates that in MY 2005 the average acre planted to upland cotton did not expect to be able to cover its cash costs with market revenue. Producing corn and soybeans, on the other hand, was expected to yield market returns well in excess of cash costs (*see* first row in red). However, when expected marketing loan subsidies are factored into farmers' expectations, the expected returns in excess of cash costs are nearly equalized for all three crops (*see* second row in yellow).

[37] Exhibit Bra-665 (Analysis of Planting Decisions Based on <u>Expected</u> Returns and <u>Cash</u> Costs).

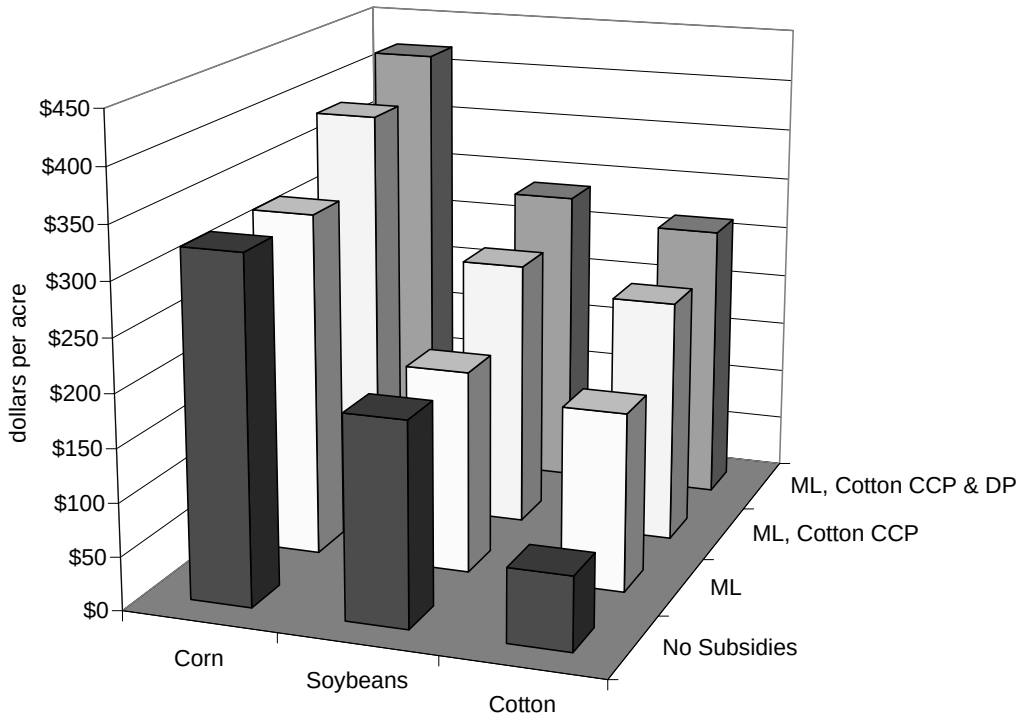
Figure 8 – Expected Returns in Excess of the Cash Costs in MY 2005 with No Cotton Marketing Loan or CCP Subsidies[38]



20. As depicted in figure 8, if upland cotton marketing loan and counter-cyclical subsidies did not exist in MY 2005, expected returns in excess of cash costs for soybeans and corn would have been much higher than for upland cotton, suggesting that many farmers would have switched to the production of alternative crops.

[38] Exhibit Bra-665 (Analysis of Planting Decisions Based on Expected Returns and Cash Costs).

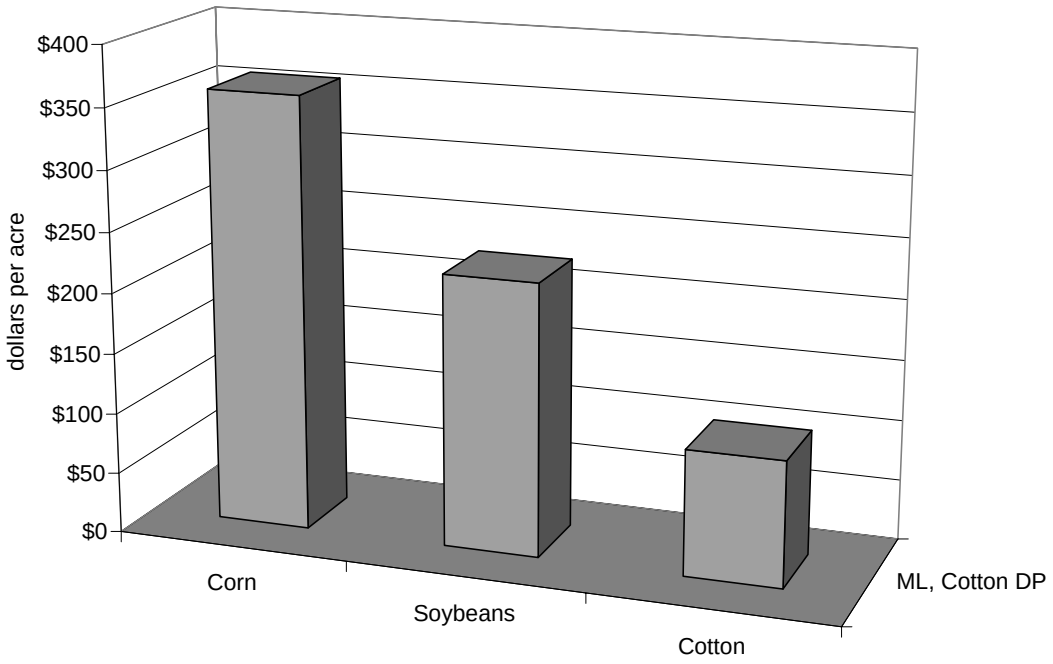
Figure 9- Expected Returns in Excess of the Cash Costs of Growing Cotton, Corn or Soybeans on a Base Acre of Cotton in MY 2007[39]



21. The first row of figure 9 shows that market returns in excess of cash costs are expected in February 2007 to be nearly five times higher for corn than for cotton and nearly three times higher for soybeans than for upland cotton in MY 2007. Considering only market returns, it would be very surprising if upland cotton acreage declined by *only* 14 percent in MY 2007, as predicted by the National Cotton Council.[40] However, when marketing loan subsidies are factored into farmers' expectations, returns for upland cotton are expected to be almost as high as those for soybeans and just 40 percent less than returns for corn.[41] Viewed in this context, it makes sense that only 14 percent of upland cotton acres switched to alternative crops.

[39] Exhibit Bra-665 (Analysis of Planting Decisions Based on Expected Returns and Cash Costs).
[40] Exhibit Bra-646 (Planting Intentions Survey, National Cotton Council).
[41] Exhibit Bra-665 (Analysis of Planting Decisions Based on Expected Returns and Cash Costs).

Figure 10 – Expected Returns in Excess of the Cash Costs in MY 2007 with No Cotton Marketing Loan and CCP Subsidies[42]

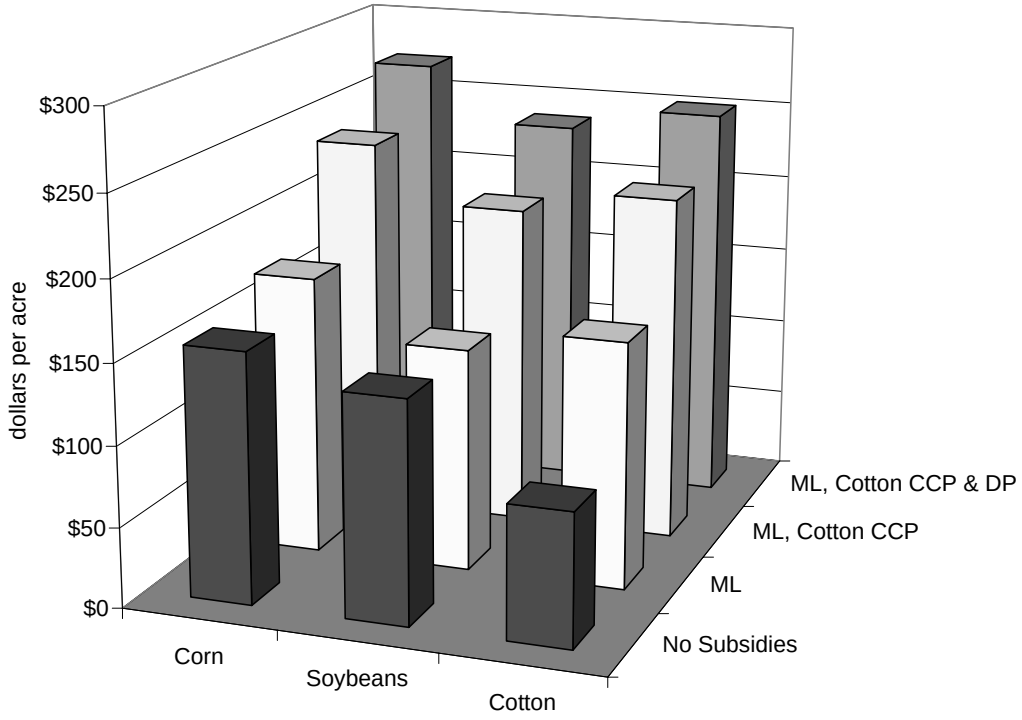


22. Figure 10 summarizes the planting decision for an acre of upland cotton base in February 2007 in the absence of upland cotton marketing loan and counter-cyclical subsidies. It again suggests that more than 14 percent of upland cotton acreage would switch to alternative crops in the absence of these subsidies.

23. As were figures 5 and 6 in Brazil's Oral Statement, the following figures 11 and 12 are based on actual market returns:

[42] Exhibit Bra-665 (Analysis of Planting Decisions Based on Expected Returns and Cash Costs).

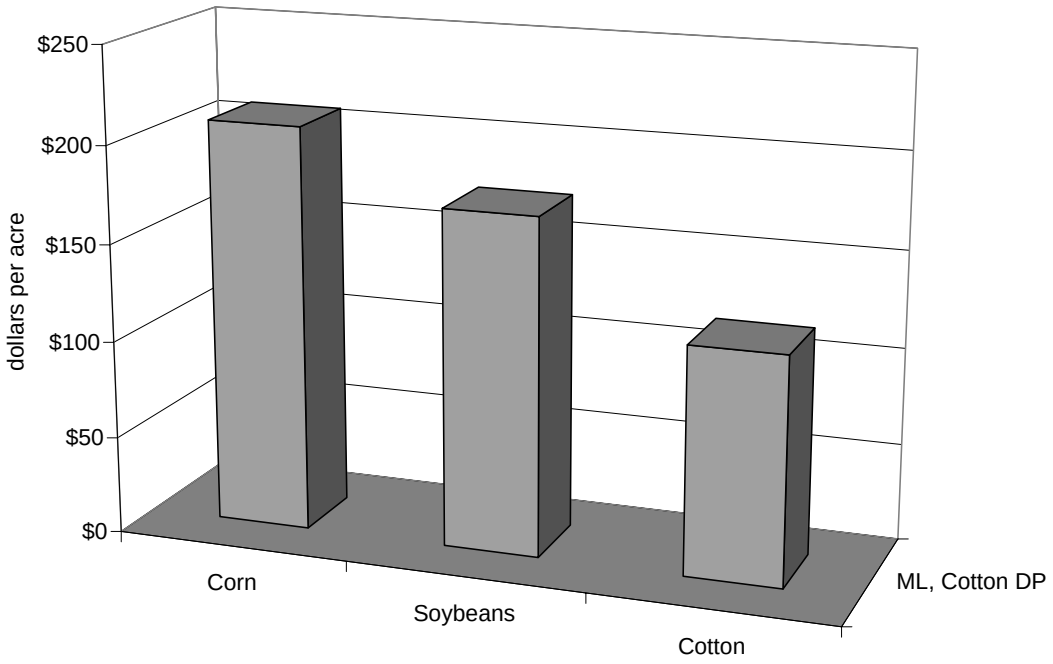
Figure 11 – Average <u>Actual Returns</u> in Excess of the Average <u>Cash Costs</u> Associated with Planting Cotton, Corn or Soybeans on an Cotton Base Acre in MY 2002-2006[43]



24. Figure 11 illustrates what actually happened between MY 2002 and 2006. The chart shows that actual market returns in excess of cash costs for upland cotton were far less than those for corn and soybeans. However, when upland cotton marketing loan subsidies are taken into account, returns in excess of cash costs were higher for upland cotton than for soybeans, and only slightly lower than for corn.

[43] Exhibit Bra-666 (<u>Actual</u> Costs and Returns Analysis Based on <u>Cash</u> Costs).

Figure 12 – Average Actual Returns in Excess of the Average Cash Costs with No Cotton Marketing Loan or CCP Subsidies in MY 2002-2006[44]



25. Figure 12 illustrates that absent upland cotton marketing loan and counter-cyclical payments, growing corn or soybeans on an upland cotton base acre would have been more profitable. Similar to Brazil's figure 6 presented as part of its Oral Statement, and based on total costs, these charts based in cash costs continue to show that planting soybeans and corn on upland cotton base acres would be attractive without price-contingent upland cotton subsidies.

26. This evidence shows that the effect of marketing loan and counter-cyclical subsidies is to provide strong financial incentives to maintain upland cotton acreage – even in the unlikely event that farmers only consider variable or cash costs when making planting decisions. *But for* the marketing loan and counter-cyclical payments for upland cotton, it would be far more profitable for upland cotton farmers, on average, to plant corn or soybeans. Thus, as Brazil indicated during the Panel Meeting, the usefulness of the comparisons based on *total* costs presented in figures 1-6 as part of its Oral Statement is not diminished by the use of cash costs in figures 7-12 above. Removing non-cash costs[45] changes the level of expected or actual market returns minus costs, but does *not* change the relative attractiveness of producing corn or soybeans – as compared to upland cotton – on a base acre of upland cotton.

[44] Exhibit Bra-666 (Actual Costs and Returns Analysis Based on Cash Costs).

[45] According to *The Commodity Costs and Returns Estimation Handbook* "noncash costs are those in which the timing of the physical use of resources and the cash payments differs." *See* Exhibit Bra-649 ("Conceptual Issues in Cost and Return Estimates," Chapter 2 of Commodity Costs and Returns Estimation Handbook, a report of the AAEA Task Force on Commodity Costs and Returns).

27. Analyzing actual and expected returns in excess of *variable* (as opposed to only *cash*) costs[46] yields a similar result. Removing fixed costs changes the level of returns minus costs, but not the relative attractiveness of growing cotton, corn or soybeans on a base acre of upland cotton. Exhibit Bra-667 provides a complete comparison of expected returns in excess of variable costs in MY 2002-2007. Exhibit Bra-668 provides a comparison of actual returns in excess of variable costs.[47]

28. The United States presented a number of other misleading arguments about U.S. upland cotton costs and returns in its Opening Statement. The United States argued that an examination of costs and returns in MY 2003 demonstrates that 92 percent of upland cotton farmers are able to cover their variable and total costs of production.[48] As Brazil explained in its Opening Statement[49], Closing Statement[50] and in response to oral questions from the compliance Panel, this assertion is misleading, and to some extent simply incorrect.

29. First, it is important to understand that the allegedly "new" cost information broken down by costs groups[51] (*i.e.*, low-, mid- and high-cost producers) is based on the same underlying survey data presented in Brazil's First Written Submission and used by Brazil in subsequent submissions and statements.[52] It is not "new," but instead an elaboration of USDA data that Brazil has relied upon throughout this proceeding. In fact, the "new" grouping of farms into those that are low-cost, mid-cost and high-cost is somewhat arbitrary. Brazil has long maintained that upland cotton producers' costs are not uniform.[53] It is entirely unremarkable that some farmers have a lower cost structure than others.

30. However, the critical flaw in the United States reliance on the "new" cost information is that it pertains to MY 2003, a year in which cotton prices were the highest they have been in the past ten years. Concluding that upland cotton farmers are generally able to cover their costs with market revenue based on market returns in MY 2003 is misleading and incorrect. In the past eight years, MY 2003 is the only year in which the average acre planted to upland cotton was able to cover its total costs of production.

31. The United States also claims that a fundamental shift occurred in the production costs of U.S. upland cotton farmers. One reason cited by the United States is the adoption of genetically engineered ("GE") cotton seeds. However, an examination of the rate of adoption of GE varieties shows that this argument, once again, is incorrect.

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[46] Variable costs include operating, land and labour costs. *See, inter alia*, Brazil's Rebuttal Submission, Sections 2.3 and 6.2.

[47] Brazil notes that the excel files in Exhibits Bra-634, 648, 665, 666, 667 and 668 easily permit an alteration of the "cost" to which market and subsidy returns are compared. The cells in the row entitled "No subsidies" in the first three worksheets can be changed to reflect different cost concepts. The charts in the later worksheets of the excel file will automatically update to reflect the new cost concept.

[48] U.S. Oral Statement, paras. 11 and 72.

[49] Brazil's Oral Statement, para. 84.

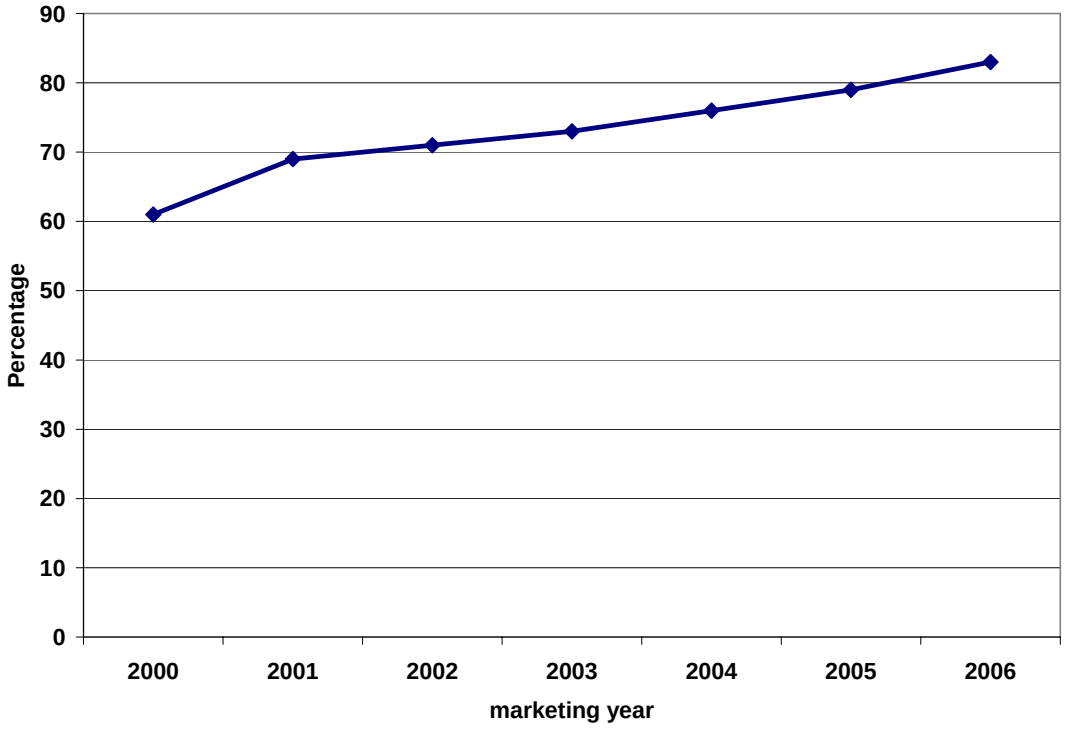
[50] Brazil's Closing Statement, paras. 15-16.

[51] Exhibit U.S.-93 (WTO Confidential).

[52] *See* Section 7.11 of Brazil's First Written Submission; Section 2.3.6 of Brazil's Rebuttal Submission; and Section 2.4 of Brazil's Oral Statement.

[53] *See, e.g.*, Brazil's Rebuttal Submission, paras. 267-272; Brazil's Oral Statement, para. 85.

Figure 13 – U.S. Adoption of GE Cotton Varieties[54]



32. The chart based on USDA data shows that the adoption of GE varieties increased from 71 percent in 2002 to 79 percent MY 2005, hardly a dramatic shift. Further, while GE varieties undoubtedly raise yields (and thus lower per-acre costs), they also increase the cost of seed, as seen in USDA's new cost survey of MY 2003. In any event, all of these developments are already reflected in the USDA's costs and return data relied upon by Brazil and the United States.

33. Moreover, the United States implies that the average profit made by upland cotton farmers in MY 2003 and the small loss in MY 2004 is the beginning of a dramatic new trend. It is not. High prices in MY 2003 allowed upland cotton farmers to cover their total costs for the first time in six years. Record high yields and a relatively high harvest price (despite lower prices in the subsequent marketing year) enabled upland cotton farmers to almost cover their costs in MY 2004. Yet, in MY 2005, despite another year of abnormally high yields, the average gap between total costs and market returns widened to $80 per acre. With lower yields and stagnant prices in MY 2006, the gap is expected to grow even wider.[55] Further, projections of future costs and market prices by USDA and FAPRI suggest that the gap between total costs and returns will continue indefinitely.[56]

34. In sum, the upland cotton cost and returns analysis presented by Brazil demonstrates that marketing loan and counter-cyclical subsidies have played a decisive role in U.S. upland cotton producers' ability to grow upland cotton profitably.

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[54] Exhibit Bra-669 ("Adoption of Genetically Engineered Crops in the U.S.: Cotton Varieties," Economic Research Service, U.S. Department of Agriculture, accessed March 2007 at http://www.ers.usda.gov/data/biotechcrops/ExtentofAdoptionTable2.htm).

[55] Exhibit Bra-648 (Actual Costs and Returns Analysis).

[56] *See, e.g.*, Brazil's First Written Submission, Figure 28 at para. 292.

5. COMMENTS BY DANIEL SUMNER

35. In this Section, Brazil presents the comments of Professor Sumner on the U.S. critique of his analysis, presented by Dr. Glauber:

36. In several documents, including the statement of Dr. Glauber[57], the United States lists what it identifies as "key problem with Brazil's new model." This same list appears in the U.S. Rebuttal Submission[58] and in U.S. responses to questions of the compliance Panel.[59] I have dealt with each of the issues listed by the United States in earlier documents. Some of the issues were discussed further at the Panel Meeting. My comments below summarize the main points with reference to floor discussion at the Panel Meeting and to earlier documents.

37. I respond to the claims of the United States in the order in which they appear in the U.S. Opening Statement.[60]

5.1. U.S. criticism: "lacks cross-commodity impacts and cross-price elasticities, potentially leading to biased price effects"[61]

38. The United States is simply wrong on this point. My model fully accounts for cross-commodity feedbacks to the cotton supply function that are relevant to assessing the impact of the removal of U.S. subsidy programs. It does so based on the U.S. supply elasticity parameter that I apply. Of course, my model does not explicitly address the effect of removing cotton subsidies on, for example, corn or hay acreage, because reporting those effects is not relevant to this proceeding. To include explicit cross-commodity impacts and cross-price elasticities in the model would only be justified if one has a policy interest in these other commodities. Yet, the impact of removing cotton subsidies on corn or hay acreage in the United States is not at issue before this compliance Panel.

39. The United States argues that leaving out these cross-commodity impacts and elasticities could "potentially" lead to bias. However, the only way that leaving out these extraneous equations could lead to "bias" with respect to the price effects for cotton is if the model used failed to incorporate feedbacks from induced changes in other crop prices on upland cotton supply. However, my model uses a supply elasticity that fully accounts for the feedback effects. This point was explicitly and clearly raised and discussed in my Annex I analysis.[62] I also discussed the issue more fully and provided citations in my rebuttal comments.[63] Finally, I reviewed these previous discussions in my supplemental statement submitted as Exhibit Bra-659.

40. While it is easy to make models more complicated, complications for their own sake are just a sign of poor modeling and a lack of understanding of the reason that models are created in the first place. The continued repetition of this claim by the United States, with no acknowledgment or engagement on the issue should not mislead the compliance Panel. The use of general equilibrium supply elasticities, such as the one I apply to my model, is well-known and well-established among modelers. There is no ambiguity on this point.

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[57] U.S. Oral Statement, Statement of Dr. Glauber, para. 3.
[58] U.S. Rebuttal Submission, Annex I, para. 4.
[59] U.S. Response to Questions of the Panel, Parts D-E, 27 February 2007, para. 35.
[60] U.S. Oral Statement, Statement of Dr. Glauber, para. 3.
[61] U.S. Oral Statement, Statement of Dr. Glauber, para. 3.
[62] "Analysis of Effects of U.S. Upland Cotton Subsidies on Upland Cotton Prices and Quantities by Daniel A. Sumner," Annex I, Brazil's First Written Submission, para. 17.
[63] "Response to the Submission of the United States titled 'Annex I: A Review of the Simulation Analysis Presented by Dr. Sumner,'" Brazil's Rebuttal Submission, Annex I, paras. 14-17.

5.2. U.S. criticism: "is static with no explicit relationship for changes in cotton stock levels and no stock's equations"[64]

41. Once again, the United States asserts that the model should have been made more complicated simply for the sake of complications. The United States does not indicate why a "dynamic" model with respect to cotton stocks would be useful in this case. Certainly there are cotton stock fluctuations from month-to-month and year-to-year, just as there are weather events and consumer trends in textile demand. The existence of stock fluctuations does not imply that such changes in stocks would be induced by the kind of policy changes under consideration here.

42. While, one could create a complicated model designed to account for these extraneous events or trends, such a model would not improve our ability to understand the effect of U.S. cotton subsidies. Indeed, introducing unnecessary complications serves only to make a model unwieldy and is likely to introduce unknown biases because it becomes impossible to trace clearly the effects of policy change.

43. In its reparameterization of my model, the United States simply uses a very large price elasticity of demand for cotton in the short run. This is a mistake. Stocks respond in the short run to unanticipated, temporary fluctuations in price, as firms liquidate stocks when prices are high in order to rebuild stocks when prices are low. Modeling endogenous stockholding may be valuable for some applications, but not for modeling policy changes that are fully anticipated and expected to be permanent.

44. Furthermore, as I explain more fully in the supplemental statement submitted as Exhibit Bra-659, the econometric exercise used to create the so-called stocks demand elasticity referred to by the United States is based on data from small year-to-year fluctuations in cotton stocks and cotton prices. The policy experiment we are considering here is far outside the range of the data used to create the estimates used by the United States. More importantly, the policy experiment we are considering here is conceptually different from the kinds of price fluctuations used to generate stock changes in the statistical exercise relied on by the United States.

5.3. U.S. criticism: "contains foreign supply elasticities that are different from FAPRI that underestimate the response of foreign producers to changes in world prices"[65]

45. I have devoted many pages to explaining the reasons for the parameter choices that are most appropriate for application in my model to estimate the effects of removing U.S. cotton subsidies on cotton market prices and quantities. An initial discussion appeared in my original Annex I analysis[66] and I included more discussion in my supplemental statement in Exhibit Bra-659. FAPRI estimates of this parameter tend to overestimate the degree of supply response to world market price changes that would be generated by a reduction in or elimination of U.S. cotton subsidies.

46. Anticipated and permanent removal of U.S. cotton subsidies would cause a substantial initial decline in U.S. cotton acreage and production. The reduced production and exports from the United States would cause higher world market prices for cotton. Foreign producers would respond to that higher world market price gradually and in a muted fashion. There are several reasons for this gradual and muted response: (i) the degree of price increase would not be known with certainty; (ii) the price received by many growers would fail to fully reflect the price change in the world market; and (iii) many growers have a limited ability to expand cotton acreage in the short run.

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[64] U.S. Oral Statement, Statement of Dr. Glauber, para. 3.

[65] U.S. Oral Statement, Statement of Dr. Glauber, para. 3.

[66] "Analysis of Effects of U.S. Upland Cotton Subsidies on Upland Cotton Prices and Quantities by Daniel A. Sumner," Annex I, Brazil's First Written Submission, paras. 20-24.

I explain these points more fully in my original Annex I analysis[67] and in subsequent documentation.[68] The United States may disagree but has provided no reasoning or evidence, other than the claim that FAPRI uses a different parameter value. That does not constitute a "key problem" with my model.

5.4. U.S. criticism: "treats production flexibility payments and direct payments differently even though they operate in the same way"[69]

47. This is a puzzling claim. Production flexibility payments applied during the period MY 1996 to 2001, and were replaced by direct payments under the provisions of the FSRI Act of 2002. Both payment programs enter the cotton supply function as a partially coupled source of revenue. The only difference in the treatment of the two programs is that I use a smaller coupling factor for production flexibility payments than I use for direct payments.

48. Throughout my analysis, going back to my analysis presented to the original panel in 2003, I explained carefully why direct payments provide larger production incentives than did production flexibility payments. I used a coupling factor of 0.15 for production flexibility payments and a coupling factor of 0.25 for direct payments. The main reason for the higher coupling factor for direct payments is that the FSRI Act of 2002 allowed producers to update their payment base for direct payments. This update of base acres has two effects. First, it tied the direct payments more closely to the actual acreage used for cotton production. Second, it enhanced growers' perceptions of the likelihood of future base acre updates, which is a major contributor to the production incentives inherent in so-called decoupled payments. I deal with this issue more fully in my 2003 article in the *Australian Journal of Agricultural and Resource Economics*.[70]

49. For the purposes of this proceeding, it is also worth reminding ourselves that production flexibility payments were discontinued in 2001 and, therefore, play little, if any, role in the results of my analysis that are relevant for the compliance Panel's assessment.

5.5. U.S. criticism: "incorporates step 2 payments directly into the producer retinal function as fully coupled payment"[71]

50. This is not a problem in my model and raising this issue suggests that the United States fails to understand some basic microeconomic principles.

51. As I explain in my Annex I analysis[72], basic microeconomic analysis confirms that taxes or subsidies applied to buyers or sellers may be analyzed as either consumer subsidies or producer subsidies at the convenience of the modeler without affecting the results of the analysis. A vertical shift down in the effective price paid by buyers (as in the case of Step 2 subsidies) may be equivalently modeled as a vertical increase of the same magnitude in the supply price received by sellers. The impacts on prices and quantities are identical no matter which way the subsidy is

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[67] "Analysis of Effects of U.S. Upland Cotton Subsidies on Upland Cotton Prices and Quantities by Daniel A. Sumner," Annex I, Brazil's First Written Submission, paras. 27-31.

[68] "Response to the Submission of the United States titled 'Annex I: A Review of the Simulation Analysis Presented by Dr. Sumner,'" Brazil's Rebuttal Submission, Annex I, paras. 20-24.

[69] U.S. Oral Statement, Statement of Dr. Glauber, para. 3.

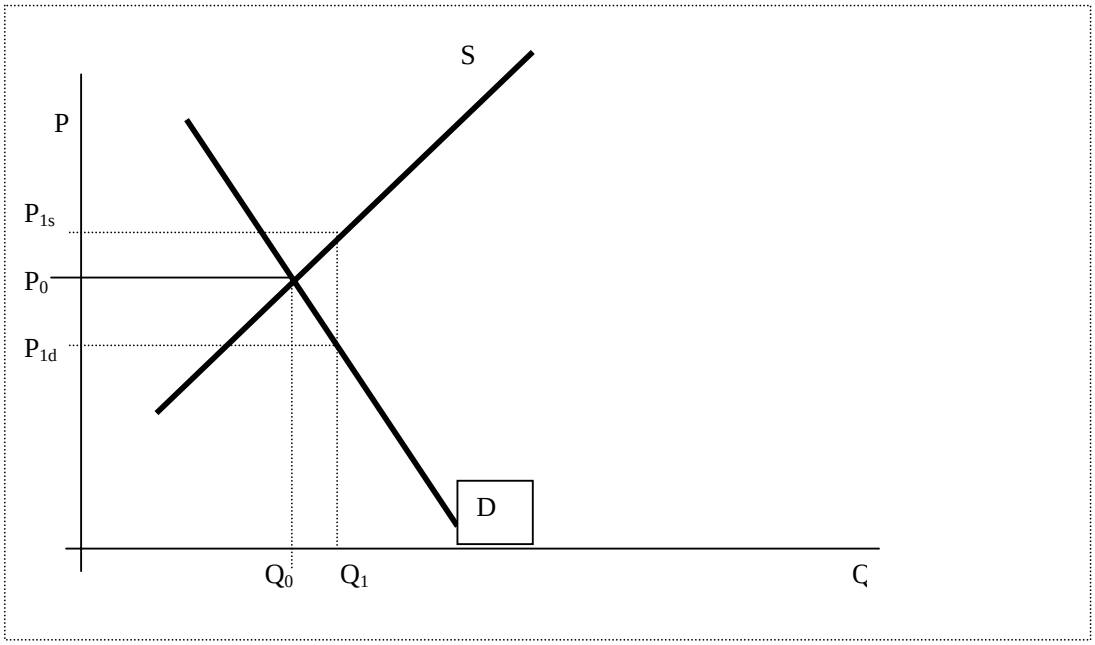
[70] Sumner, Daniel. "Implications of the US Farm Bill of 2002 for Agricultural Trade and Negotiations." *The Australian Journal of Agricultural and Resources Economics*, Volume 47, Number 1, March 2003, pp. 99-122.

[71] U.S. Oral Statement, Statement of Dr. Glauber, para. 3.

[72] "Analysis of Effects of U.S. Upland Cotton Subsidies on Upland Cotton Prices and Quantities by Daniel A. Sumner," Annex I, Brazil's First Written Submission, paras. 54-56.

incorporated in the analysis. This is a standard exercise on the incidence of taxation (negative subsidy) for undergraduate students in microeconomics.[73]

Figure 14 – Simple Graphical Demonstration of the Equivalence of a Production or Demand Subsidy



52. In Figure 14, a demand subsidy is shown as a lower effective price paid by buyers in the amount of $P_0 - P_{1d}$. This lower effective price (which includes the subsidy) elicits a higher quantity demanded Q_1. In order to encourage that amount of additional production, the market price must rise to P_{1s} (the new price received by producers). Thus, the demand subsidy causes the market price received by producers to rise to P_{1s}, while the price paid by buyers falls to P_{1d}. The amount of the subsidy is $P_{1s} - P_{1d}$. Alternatively, if a subsidy of this amount is paid to producers, the quantity supplied would rise to Q_1, the net price received by producers (inclusive of the subsidy) would be P_{1s} and the price paid by buyers would be P_{1d}. The equilibrium results are identical to those that would be obtained if the subsidy were initially provided to buyers. The net result in terms of price and quantity effects of the subsidy depends on the magnitude of the per-unit subsidy and the supply and demand slopes, or elasticities.

53. This conceptual framework is directly applied to my modeling of the Step 2 program. The results of my analysis would be identical whether the subsidy enters the model on the demand side or the supply side. Thus, the United States has not identified a "key problem." Rather, it has identified a natural modeling approach that I used to make the analysis transparent and straightforward.

54. Finally, I note that the United States' arguments do not affect my results from removing marketing loan and counter-cyclical subsidies only, which are the most relevant simulation results for the compliance Panel's assessment.

[73] *See* Robert S. Pindyck. and Daniel L. Rubinfeld, *Microeconomics*, fifth edition Prentice Hall, 2001, pages 313-320. See also exercise 13, page 323.

5.6. U.S. criticism: "appears to ignore statutory parameters, for example by including countercyclical payment rates in each of the various price expectations that sometimes exceed statutory maximum. The maximum countercyclical payment paid on 85 percent of pace and program yields cannot exceed 13.7 three cents. Yet Dr. Sumner incorporates a value as high as 19.10 cents, which is 39 percent greater than the maximum allowed rate"[74]

55. The United States is also in error on this point. As I explained briefly in my oral remarks[75], the United States failed to read with care the second Appendix of my Annex I analysis, where my approach to modeling counter-cyclical payments is discussed in detail. In particular, Table A.4, on page 45 of my Annex I analysis, explicitly and clearly shows the projected counter-cyclical payment rate per unit of *output*.[76] The statutory maximum applies to counter-cyclical program payments per unit of *program base*. Hence, there is no conflict. My projected counter-cyclical payment rate per unit of *output* is independent from the statutory limit placed on the counter-cyclical payment rate per unit of *program base*. In particular, because counter-cyclical payment base exceeds production, we expect the counter-cyclical payment rate per unit of output to be larger than the counter-cyclical payment rate per unit of base.

5.7. Conclusion

56. In sum, during the Panel Meeting, the United States has again criticized my model, but not identified any real problems. Its repeated criticism result from a number of obvious U.S. errors that I addressed above. In some cases, the United States also simply repeats criticisms with no acknowledgment of my earlier responses thereto.

6. CONCLUSION

57. Brazil looks forward to answering the forthcoming questions posed by the Panel.

[74] U.S. Oral Statement, Statement of Dr. Glauber, para. 3.
[75] Brazil's Oral Statement, para. 120.
[76] "Analysis of Effects of U.S. Upland Cotton Subsidies on Upland Cotton Prices and Quantities by Daniel A. Sumner," Annex I, Brazil's First Written Submission.

ANNEX D-5

COMMENTS OF THE UNITED STATES ON THE ORAL STATEMENTS OF BRAZIL AT THE MEETING WITH THE PANEL

(9 March 2007)

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131	Export Finance and Insurance Corporation (Australia) - Mission and Objectives; http://www.efic.gov.au/static/efi/corporateinfo/mission.htm Overview of EFIC's role; http://www.efic.gov.au/static/efi/corporateinfo/governance.htm
132	AuslandsGeschaftsAbsicherung der Budesrepublik Deutschland, Federal Export Credit Guarantees, Basics: Main Features of Export Credit Cover; http://www.agaportal.de/en/aga/grundzuege/grundzuege_exportkredit.html
133	Korea Export Insurance Corporation , preface (emphasis added); http://www.keic.or.kr/homepage2/english/main.html.; East-West Debt: "about the Korea Export Insurance Corporation"; http://www.eastwest.be/east_west/keic.htm
134	Bancomext 2005 Annual Report, pp. 2, 26; http://www.bancomext.com/Bancomext/publicasecciones/secciones/7304/AnnualReportBancomext2005.pdf
135	Daily A-Index and NY Futures Price Data
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137	Cecil Davison and Brad Crowder, "Northeast Soybean Acreage Response Using Expected Net Returns" *Northeastern Journal of Agriculture and Resource Economics*, April 1991
138	Duncan M. Chembezi and Abner W. Womack, "Regional Acreage Response for U.S. Corn and Wheat: The Effects of Government Programs", *Southern Journal of Agricultural Economics*, July 1992
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Short Form	Full Citation
Brazil – Aircraft (Article 21.5 II)	Panel Report, *Brazil – Export Financing Program for Aircraft – Second Recourse by Canada to Article 21.5 of the DSU*, WT/DS46/RW/2, adopted August 23, 2001
Canada – Aircraft (AB)	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999
Canada – Aircraft II	Panel Report, *Canada – Export Credits and Loan Guarantees for Regional Aircraft*, WT/DS222/R, adopted 19 February 2002
EC – DRAMs	Panel Report, *European Communities – Countervailing Measures on Dynamic Random Access Memory Chips from Korea*, WT/DS299/R, adopted 3 August 2005
Korea – Commercial Vessels	Panel Report, *Korea – Measures Affecting Trade in Commercial Vessels*, WT/DS273/R, adopted 11 April 2005
US – Upland Cotton (AB)	Appellate Body Report, *United States – Subsidies on Upland Cotton*, WT/DS267/AB/R, adopted 21 March 2005

I. INTRODUCTION

1. The United States appreciates the opportunity provided by the Panel to comment on Brazil's "oral" presentation at the meeting with the Panel. In that meeting, Brazil not only presented 77 pages of arguments and evidence orally over the course of approximately four and a half hours – unilaterally consuming almost the entire first day of the meeting with the Panel – but it also submitted 42 new "exhibits" (and 9 resubmitted exhibits) containing information that Brazil did *not* present orally but simply attached to its oral statement.

2. The "exhibits" included with Brazil's oral statement include a third written submission produced by Brazil allegedly to address issues "which there was not time to discuss in [Brazil's economists'] brief statement before the Panel."[1] Leaving aside the irony of describing a four and a half hour oral presentation – of which a substantial portion was taken up by Brazil's economist – as "brief," Brazil's written submission was made in breach of the Panel's working procedures. The working procedures provide for two written submissions, a first written submission and a rebuttal submission, both of which are to be submitted "[b]efore the substantive meeting of the Panel with the parties to the dispute."[2] The working procedures do not contemplate any third written submission either in or after the meeting of the Panel with the parties. While the Panel's working procedures do contemplate – indeed, require – that the parties submit a written product either at or shortly after the meeting with the Panel, the procedures are very clear as to what that written product must be. Specifically, parties must submit "a written version *of their oral statement*" presented to the Panel and the other parties during the meeting.[3] The Panel's working procedures neither contemplate nor permit the submission of arguments and evidence which were *not* part of any oral statement ("which there was [allegedly] not time to discuss in" an oral presentation that otherwise spanned almost an entire day).[4] Given that the third written submission in BRA-659 is not permitted under the Panel's working procedures, the United States respectfully requests that the Panel reject that submission.

3. The United States also notes that much of the new evidence and arguments presented by Brazil in its oral statement was known and available to Brazil well before the date of the Panel meeting. Yet Brazil appears to have chosen to withhold it until the meeting with the Panel when little time remained to subject it to scrutiny. Upon review of this new evidence and argument, it is apparent why Brazil would be anxious to avoid any meaningful assessment thereof.[5] Although voluminous, this evidence and argument offer little support for Brazil's claims. In fact, much of the data newly submitted by Brazil confirms the U.S. arguments that the United States has complied with its obligations to implement the DSB's recommendations and rulings.

II. THE EXPORT CREDIT GUARANTEE PROGRAMS MEET THE TESTS IN THE SCM AGREEMENT FOR NOT BEING EXPORT SUBSIDIES

4. In the case of the export credit guarantees, the fact remains that:

- the United States has provided no GSM 103 guarantees since 1 July 2005;

[1] *See* Supplementary Statement of Daniel Sumner, para. 1 (Exhibit BRA-659).

[2] *See* United States – Subsidies on Upland Cotton (DS267), Working Procedures for the Panel, para. 4 (8 November 2006).

[3] *See* United States – Subsidies on Upland Cotton (DS267), Working Procedures for the Panel, para. 4 (8 November 2006).

[4] *See* Supplementary Statement of Daniel Sumner, para. 1 (Exhibit BRA-659).

[5] In this regard, the United States recalls Brazil's efforts at the Panel meeting and thereafter to preclude or limit any opportunity for the United States to respond in writing to Brazil's "oral" presentation.

- the United States has provided no Supplier Credit Guarantee Program (or "SCGP") guarantees since 1 October 2005 and there are, presently, no longer any guarantees even "outstanding" under that program;

- following carefully the guidance provided by the original panel, the United States imposed a new fee schedule with respect to GSM-102 guarantees under which higher fees are assessed for obligations in higher-risk countries;

- the United States reclassified into an ineligible risk category twenty-two countries posing a higher risk of default that had been eligible for GSM-102 guarantees before 1 July 2005;

- as a result of the changes in the fee schedule, fees have increased 46 percent on average over fiscal year 2004, the last year in which the old fee schedule applied;

- all of the U.S. changes, together, increased the premiums and decreased the likelihood of incurring substantial operating costs and losses over the long-term of the portfolio of programs examined by the original panel; and

- according to the U.S. budget data, premiums under the three U.S. export credit guarantee programs were more than adequate to cover their long-term operating costs and losses even before the United States took steps to implement the DSB's recommendations and rulings and are even more assured of doing so in the future given all of the changes made by the United States.

5. The substantial evidence before the Panel thus shows that the United States is not providing any export subsidies within the meaning of item (j) in Annex I of the *Agreement on Subsidies and Countervailing Measures* ("SCM Agreement"). Under the proper interpretation of the *SCM Agreement*, the assessment of whether or not export credit guarantees constitute prohibited export subsidies can – indeed should – begin and end with that assessment under item (j).

6. Nothing in Brazil's oral presentation – nor in any of its submissions prior to that – undermine the evidence of profitability before the Panel or the fact that the U.S. export credit guarantee programs are entirely consistent with item (j) of the Illustrative List.[6] Rather, Brazil seeks to invent new obligations not provided for in the *SCM Agreement*, in particular, by asserting a separate standard for "export subsidy" under the general definitional elements of Articles 1.1 and 3.1(a). Even leaving aside that Brazil's approach is unsupported by the text, that approach fails even on its own terms.

A. <u>There Is No Difference Between the Amount Paid On Loans Subject to a GSM-102 Guarantee and Other Comparable Commercial Loans</u>

7. The substantial evidence before the Panel, thus, shows that the United States is not providing any export subsidies within the meaning of item (j). In the view of the United States, under a proper

[6] The United States does not address here Brazil's arguments attempting to undermine the substantial evidence showing that the U.S. export credit guarantee programs have historically been profitable even without the recent changes made to implement the recommendations and rulings of the DSB. Nor does the United States address Brazil's arguments about export credit guarantees issued prior to 1 July 2005 and rescheduled debt. Brazil's oral presentation contain nothing new in respect of those arguments and the United States has them in its submissions already before the Panel. The U.S. arguments can be found in the U.S. first written submission at paragraphs 71-104, the U.S. Rebuttal Submission at paragraphs 84-133, and the U.S. oral statement at paragraphs 16-49.

interpretation of *SCM Agreement*, the assessment of whether or not export credit guarantees constitute prohibited export subsidies begins and ends with that assessment under item (j).

8. Nothing in Brazil's oral presentation – nor in any of its prior submissions – undermine the evidence of profitability before the Panel or the fact that the United States export credit guarantee programs are entirely consistent with item (j) of the Illustrative List. Rather, Brazil seeks to invent new obligations not provided for in the *SCM Agreement*, in particular, by asserting a separate standard for "export subsidy" under the general definitional elements of Articles 1.1 and 3.1(a). Even leaving aside that Brazil's approach is unsupported by the text, that approach fails even on its own terms.

B. Brazil Fails to Show That There Is a Difference Between the Amount Paid on Loans Subject to a GSM-102 Guarantee and Other Comparable Commercial Loans, and Fails to Rebut the U.S. Evidence in this Regard

9. Article 14 of the *SCM Agreement* sets out the conditions under which a "benefit" may be considered to be "conferred" for countervailing duty purposes and defines how to measure "benefit" in such a case. While Article 14 does not apply directly in the case of actions under Part II of the *SCM Agreement*, it interprets and applies the definition of "benefit" set out in Article 1.1. Thus, the Appellate Body has relied upon Article 14 as important contextual guidance in interpreting "benefit."[7] Indeed, its was Brazil that originally invoked Article 14 to justify its prohibited export subsidy arguments against the export credit guarantees in the present proceeding.[8]

10. Paragraph (c) of Article 14 provides that a government-provided loan guarantee confers a benefit for countervailing duty purposes *only* where there is "a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee." The "benefit" is measured as "the difference between these two amounts adjusted for any differences in fees."

11. Even by this standard, however, Brazil fails to show that the U.S. GSM-102 guarantees constitute prohibited export subsidies. In fact, Brazil does not submit a single piece of evidence to show – with respect to *any* loans subject to a GSM-102 guarantee – that there is "a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee."

12. Moreover, Brazil has failed to rebut the U.S. evidence showing that commercial lenders regularly involved in both the GSM-102 program and other lending in the foreign agricultural sector, in fact, do provide – and have provided – unsecured financing to foreign banks that are CCC-approved obligors on terms the annualized cost of which was less than that available under the GSM-102 program.[9] In fact, Mr. Sundaram, the consultant retained by Brazil for purposes of this proceeding, acknowledged that the examples the United States provided, as supplied by [[ ]], show "lower annualized costs than under GSM-102."[10]

13. While Mr. Sundaram went on to criticize the U.S. examples, his criticism is without basis. According to Mr. Sundaram, the "average life" is allegedly insufficient to capture some hypothesized riskiness that is greater in a three-year term GSM transaction than in a two year bullet payment.[11] However, in each of the examples provided by the United States, the short-term and long-term ratings

[7] *Canada – Aircraft (AB)*, para. 155.

[8] Brazil First Written Submission, paras. 371-375

[9] U.S. First Written Submission, paras. 119-130 and Exhibit US-22; U.S. Rebuttal Submission, paras. 145-170.

[10] Brazil Oral Statement, para. 214

[11] Brazil Oral Statement, para. 219

for each of the banks are comparable.[12] Indeed, Mr. Sundaram acknowledged that the Panamanian and Mexican banks are both "investment grade."[13] Thus, the theoretical difficulty that Brazil tries to create is inapplicable to those comparisons as a matter of fact. Despite Brazil's allegations to the contrary[14], the comparisons offered by the United States are fully "apples-to-apples" comparisons.

14. Moreover, Brazil appears to ignore the pricing of risk inherent in the transactions. While it emphasizes that "fully one-third of the principal remains at risk after two years"[15] in a GSM-guaranteed transaction, Brazil fails to acknowledge that *fully one-third of the principal has been paid* after *one* year in the same transaction. In contrast, the entire bullet payment remains outstanding for the first two years. As a matter of commercial logic, the risk inherent in an obligor's capacity to service debt increases with the amount of debt outstanding. The repayment term of the GSM transaction compels an early payment of principal reducing the outstanding debt.[16]

15. Finally, the United States notes Brazil's assertion that "the examples provided by the United States do not appear to prove anything about the ability of GSM-102's target foreign obligors [allegedly non-investment grade] to secure foreign credit."[17] However, this assertion serves to undermine what has been Brazil's own – entirely unfounded – argument in this proceeding; namely, that the United States allegedly "targets" and services only non-investment grade foreign obligors. The United States welcomes Brazil's acknowledgment that GSM credit guarantees are offered in *many* markets where other financing is readily obtained, including in Mexico and Panama – two of the countries involved in the examples provided by the United States. And the U.S. examples are not the only ones involving investment grade participants in the GSM program; scores of CCC-approved foreign bank obligors enjoy an investment grade rating.[18] Brazil's sweeping assertions that GSM-102 guarantees are provided only where there is no financing available to foreign obligors is undermined not only by the particular examples provided by the United States, but also by this evidence of the large number of investment-grade participants.

C. There is No Basis to Ignore All of Textual Provisions Dealing With Export Credit Guarantees and Loan Guarantees and to Use Instead a "Severable Benefit" Approach Specifically Precluded Under the *SCM Agreement* With Respect to Such Measures

16. Unable to make its case under *any* provision of the *SCM Agreement* dealing either with export credit guarantees or loan guarantees, Brazil essentially asks the Panel to ignore the *SCM Agreement* altogether and to create and impose obligations not found anywhere in the text. Towards this end, Brazil argues that other panels have disregarded the text as well. Brazil's arguments are simply not tenable.

17. Brazil asserts, for example, that the panel in *EC-DRAMs* "agreed that a government guarantee confers a 'benefit' *per se* if without the guarantee, commercial lending would not have been available. Where commercial lending would not have been available without the government guarantee, the panel in *EC-DRAMs* did not require the type of quantitative assessment on which the United States here insists."[19] As a threshold matter, however, that panel did not – indeed, could not – "undo" the disciplines agreed upon in Article 14(c) of the *SCM Agreement*. To the contrary, the *EC-DRAMs*

[12] U.S. Rebuttal Submission, para. 150.

[13] Brazil Oral Statement, para. 223.

[14] Brazil Oral Statement, para. 222.

[15] Brazil Oral Statement, para. 221.

[16] In fact, GSM-102 guarantees often require semi-annual payments of principal.

[17] Brazil Oral Statement, para. 223. Brazil appears to make the same incorrect and irrelevant point in paragraph 177 of its oral statement.

[18] U.S. First Written Submission, para. 110.

[19] Brazil Oral Statement, para. 194.

panel expressly *acknowledged* the proper approach for the determination of "benefit" in the context of a government guaranteed loan in Article 14(c) of the *SCM Agreement*: "[I]t appears that the examination is to focus on the difference between the amount paid on a loan guaranteed by the government, compared to the amount that would have to be paid on a comparable commercial loan, absent the government guarantee."[20] The panel's ultimate finding – that the EC could properly find a "benefit" where there was no "evidence on the record . . . to contradict the EC's conclusion that, absent the government guarantee, the banks would not have been willing to agree to the [financing] at all"[21] – is entirely consistent with the standard in Article 14(c) of the *SCM Agreement*. But the facts of that dispute are not the same as the facts before this Panel. As the United States has shown, this is *not* a situation where "absent the government guarantee" banks "would not have been willing to agree to . . . [financing] at all."

18. Brazil also cites the panel report in *Canada-Aircraft II* for the proposition that "even in assessing 'benefit' under Article 14(c), the legal standard boiled down to an assessment whether fees for the government guarantee were consistent with fees for commercial guarantees."[22] There, too, however, the panel expressly acknowledged that the appropriate standard was set out in Article 14(c) of the *SCM Agreement*. The panel found that under the circumstances of that dispute, it was "safe to assume" that it the fees charged for the loan guarantee were not "market based," the test in Article 14(c) would be met. Moreover, even while it asserted that it was "safe" to make such an assumption, the panel actually *required* Brazil, as the complaining party, to provide "arguments or information regarding what the [airline] might have had to pay on a *comparable commercial loan* absent the *IQ* loan guarantee."[23] The panel noted that:

> Brazil has made no arguments to the effect that 'there is a difference between the amount that the [Mesa Air Group] pays on a loan guaranteed by [IQ] and the amount that the [Mesa Air Group] would pay on a comparable commercial loan absent the [IQ] guarantee', adjusted for any difference in fees. In particular, although Brazil does not deny that loan guarantees are available on a commercial basis, Brazil has failed to adduce any arguments or information regarding what Mesa Air Group might have had to pay on a comparable commercial loan absent the IQ loan guarantee.[24]

19. On the basis of *that* failure on the part of Brazil – as well as Brazil's failure to "make any other argument to the effect that IQ's fee for its loan guarantee to Mesa Air Group is not market based" – the panel "reject[ed] Brazil's claim that the IQ loan guarantee to Mesa Air Group confers a 'benefit.'"[25]

20. Brazil has, thus, failed to provide any basis for the panel to disregard all of the textual provisions relating to export credit guarantees and loan guarantees and to use, instead, its "severable benefit" approach. As the United States explained in the meeting with the Panel, Brazil's approach fundamentally undermines the drafters' acknowledgment, expressed in Article 14(c), that the provision of a loan guarantee is fundamentally different from the provision of other government services. While a comparison of fees for a government service against the fees charged in the market for a comparable service is the proper approach in the case of other government services – as provided in Article 14(d) – Article 14(c) specifically *precludes* such an approach for loan guarantees. Instead, it recognizes that a loan guarantee is made for the sole purpose of *supporting a loan transaction*; the guarantee becomes an integral part of that transaction and has no value beyond it. An assessment of the total costs of the transaction is necessary to assess whether a "benefit" is actually conferred by the

[20] *EC-DRAMs*, para. 7.190.
[21] *EC-DRAMs*, para. 7.190.
[22] Rebuttal Submission of Brazil, para. 410.
[23] *Canada-Aircraft II*, para. 7.399 (emphasis added).
[24] *Canada-Aircraft II*, para. 7.399.
[25] *Canada-Aircraft II*, para. 7.399.

guarantee. A simple comparison of the fee charged for the issuance of one loan guarantee to the fee charged for another may provide an incomplete and distorted picture in this regard.

D. Brazil's Argument That GSM-102 Guarantees Necessarily Provide a Benefit Because They Constitute a "Unique Financial Instrument" Is Legally and Factually Unfounded

21. In its oral presentation, Brazil once again asserts that the GSM-102 export credit guarantee is "a unique financial instrument without any parallel at market."[26] In Brazil's view, "that is the beginning and end of the analysis" and demonstrates that the GSM-102 program confers benefits *per se*.[27] Brazil has not shown any textual basis for this kind of *per se* test.

22. Indeed, the United States wonders if Brazil has thought through fully the consequences of its argument. If the *SCM Agreement* were found to actually contain the standard advocated by Brazil, one would have expected *Brazil – Aircraft (Article 21.5 II)* to have been decided differently. There, Canada challenged certain "PROEX" interest rate equalization payments made "in support of export credits extended to the purchaser, and not to the producer, of Brazilian regional aircraft."[28] The panel noted that, in those circumstances, Canada could make a *prima facie* showing of "benefit" if it established that "PROEX III payments allow the purchasers of a product to obtain export credits on terms more favourable than those available to them in the market, this will, at a minimum, represent a prima facie case that the payments confer a benefit on the producers of that product as well, as it lowers the cost of the product to their purchasers and thus makes their product more attractive relative to competing products."[29] The panel did not consider whether PROEX payments were a "unique financial instrument." Brazil did not argue there, as it has attempted to do here, that "the beginning and end of the analysis" was the question of whether PROEX III payments were "a unique financial instrument without any parallel at market."[30] Indeed, that question could presumably have been answered fairly easily, because unlike PROEX, commercial actors are not in the business of making payments for nothing.

23. In any event, the United States has provided examples of other international financial institutions – such as such as the European Bank for Reconstruction and Development ("EBRD"), the International Finance Corporation ("IFC"), and the Inter-American Development Bank ("IDB") – that provide similar guarantees to the GSM-102. While Brazil attempts to dismiss these examples by arguing that these entities cannot, by definition, provide commercial products, Brazil's argument is without merit.[31] As the principal basis for this argument, Brazil continues to focus on the ability of such entities to "borrow from government treasuries," asserting that "as a result, public entities tend to enjoy a lower cost of funds than their market-based counterparts."[32] Brazil further suggests that these entities cannot provide commercial products because they "enjoy a guarantee flowing from the full faith and credit of governments."[33]

24. However, Brazil has not shown that the entities identified by the United States rely on such borrowing for their operations or that they enjoy such guarantees from governments. The IFC, for example, receives no sovereign guarantee.[34] Furthermore, the IFC indicates that "the major source of IFC's borrowings is the international capital markets. Under the Articles of Agreement, the

[26] Oral Statement of Brazil, para. 174.
[27] Oral Statement of Brazil, para. 174.
[28] *Brazil – Aircraft (Article 21.5 II)*, para. 5.28, n. 42.
[29] *Brazil – Aircraft (Article 21.5 II)*, para. 5.28, n. 42.
[30] Oral Statement of Brazil, para. 174.
[31] Brazil Oral Statement, para. 187.
[32] Brazil Oral Statement, para. 188.
[33] Brazil Oral Statement, para. 188.
[34] U.S. Rebuttal Submission, para. 166.

Corporation may borrow in the public markets of a member country only with approvals from that member and also the member in whose currency is denominated."[35] Further, "market borrowings are generally swapped into floating-rate obligations denominated in US dollars."[36] EBRD issues medium and long-term debt obligations on the market.[37]

25. Moreover, the ability of an entity to borrow from a government does not necessarily preclude an entity from providing *products* on commercial terms.[38] For example, the panel recognized in *Korea – Commercial Vessels* that:

> The fact that KEXIM may receive subsidized government funding does not mean that it will inevitably provide subsidized financing to its customers. It is possible that KEXIM might charge market rates and increase its profit margin instead."[39]

26. Brazil also asserts that a former U.S. official – specifically, a former Secretary of the U.S. Treasury – has recognized that international financial institutions cannot offer commercial products.[40] However, Brazil's own exhibit shows that the statement referenced by Brazil did *not* relate to any of the international financial institutions noted above, but, rather, to state-owned or controlled "market window" institutions of individual OECD members that restrict financing to national exporters. International financial institutions such as IFC, IDB, and EBRD are fundamentally different entities. They do not operate at the behest of any single government. Indeed, Brazil itself has noted that the IDB is owned by 47 member countries[41]; EBRD by 60 governments[42]; and IFC by 178 member countries.[43] Rather, they operate commercially without benefitting any particular government or citizen constituency. Brazil has provided no legitimate basis for asserting that such financial institutions can never provide commercial products.

27. In short, Brazil fails to show *either* that its "unique financial instrument" test is required under the *SCM Agreement* or that the measures it challenges are in fact "unique financial instruments."

E. Brazil's Argument Would Effectively Render Most, If Not All, Export Credit Guarantees Prohibited Export Subsidies

28. Brazil's ultimate argument appears to be that export credit guarantees are prohibited export subsidies unless there is a purely private bank (like a Citibank, for example) already providing the same export credit guarantees and, even in that case, the guarantees are prohibited subsidies unless the *fees* charged by the private bank for the export credit guarantees are lower than the *fees* charged by the government entity. These assertions are without basis in the *SCM Agreement* and, given the nature of the market for export credit guarantees, would effectively render *all* export credit guarantees provided by any Member anywhere in the world to be prohibited subsidies.

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[35] Exhibit US-79, p. 13.
[36] Exhibit US-79, p. 13.
[37] Exhibit US-77, p.10.
[38] U.S. Rebuttal Submission, para. 156.
[39] *Korea – Commercial Vessels*, para. 7.84.
[40] Brazil Oral Statement, para. 186 and Exhibit Bra-654.
[41] Rebuttal Submission of Brazil, para. 442.
[42] Rebuttal Submission of Brazil, para. 441.
[43] Rebuttal Submission of Brazil, para. 440. Brazil also criticizes the United States for finding "significance in that fact that public entities like the EBRD, IDB and IFC are 'profitable'."Brazil Oral Statement, para. 189. The United States, however, was merely responding to the significance that *Brazil* had ascribed to its assertion that such institutions are incapable of providing commercial products because they are "not a private sector actor motivated by profit." Rebuttal Submission of Brazil, para. 441.

29. As Brazil is well aware, export credit guarantees and other similar loan guarantees are now and have always been instruments provided predominantly – if not exclusively – by governments and international financial institutions, as opposed to purely private banking institutions. It is hardly surprising then that Members would have agreed to a standard for "prohibited export subsidy" in item (j) that imposes disciplines based on the net costs of a program.[44] Nor is it surprising that, in the context of countervailing duty investigations, Members would have agreed to a standard that looks to the effect of a guarantee on the underlying loan. Brazil's efforts to have the Panel ignore the text itself – what Members actually agreed to given the particular nature of the measure and the market – and to impose instead a fee-based comparison to some theoretical purely private bank is untenable.

30. This would effectively render most if not all export credit guarantees to be prohibited export subsidies, in contravention of the express intent of the drafters in item (j) and Article 14(c) of the *SCM Agreement*. Furthermore, Brazil's approach is contradicted by Article 10.2 of the *Agreement on Agriculture*. If the test for being a prohibited export subsidy were as simple as Brazil claims, then there would have been no need for the negotiators of the WTO agreements to have specifically called for the development of international disciplines on export credit guarantees. Indeed, by calling for the development of additional disciplines on export credit guarantees, Article 10.2 of the *Agreement on Agriculture* supports the fact that at present the analysis can – indeed should – begin and end with the disciplines currently in item (j).

31. The ramifications of such an impermissible interpretation are significant. The compliance panel will recall India provides similar services through the Export Credit Guarantee Corporation of India, Ltd. Further examples include the following:

- The Export Finance and Insurance Corporation of Australia, which offers export credit insurance (also subject to item(j)) "when the private market lacks capacity or willingness, filling the market gap."[45] EFIC operates "primarily in that part of the market that is not served by the private market."[46]

- Euler Hermes, the provider of export credit guarantees for the Federal Republic of Germany, provides such products "to support German enterprises to open difficult markets."[47]

- The Korea Export Insurance Corporation – an official export credit agency of Korea – provides "agro-fishery" export insurance that "compensates the losses arising from export transactions and overseas investments that *cannot be handled by the general insurance systems*."[48]

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[44] The United States notes in this regard that in the Illustrative List to the Tokyo Round Subsidies Code, item (j) provided that premium rates could not be "*manifestly* inadequate operating costs and losses of the programs." (Emphasis added). In the Uruguay Round, the negotiators deleted the word "manifestly" from item (j). It is difficult to accept that the negotiators would have gone to the trouble of modifying the standard in item (j) if, as argued by Brazil, that standard could readily be ignored in favour of a different standard.

[45] Export Finance and Insurance Corporation (Australia) - Mission and Objectives; http://www.efic.gov.au/static/efi/corporateinfo/mission.htm (Exhibit US-131).

[46] Export Finance and Insurance Corporation (Australia) - Mission and Objectives; http://www.efic.gov.au/static/efi/corporateinfo/mission.htm (Exhibit US-131).

[47] AuslandsGeschaftsAbsicherung der Budesrepublik Deutschland, Federal Export Credit Guarantees, Basics: Main Features of Export Credit Cover; http://www.agaportal.de/en/aga/grundzuege/grundzuege_exportkredit.html (Exhibit US-132).

[48] Korea Export Insurance Corporation, preface (emphasis added); http://www.keic.or.kr/homepage2/english/main.html. (Exhibit US-133); *see also* East-West Debt: "about the Korea Export Insurance Corporation" http://www.eastwest.be/east_west/keic.htm (Exhibit US-133).

- Banco Nacional de Comercio Exterior of Mexico, a bank "owned by the Mexican government, offers "export credit insurance to cover Mexican firms against default of credit sales to foreign [] customers."[49]

32. Are each of these Members, as well as scores of other Members, breaching their WTO obligations simply because purely private banks do not now, and have not historically, operated in this particular segment of the market? Brazil has utterly failed to show anything in the text of the *SCM Agreement* indicating that Members agreed upon such an absurd result.

33. The text confirms, instead, that the standards reflected in item (j) provide the exclusive test for whether export credit guarantees provide prohibited export subsidies. As discussed above, in the U.S. submissions, and in the meeting with the Panel, the U.S. budget data show – definitively – that premiums collected under the U.S. export credit guarantee program are more than adequate to cover the long-term operating costs and losses of the programs. In short, the United States is fully in compliance with the standard in item (j).

III. BRAZIL HAS FAILED TO ESTABLISH ITS CLAIMS REGARDING THE STEP 2, MARKETING LOAN, AND COUNTER-CYCLICAL PAYMENT PROGRAMS AND ALL PAYMENTS THEREUNDER

34. Brazil's "oral" presentation also fails to remedy the fact that Brazil has provided virtually *no empirical evidence* to support its claims that (a) termination of the Step 2 program "will likely have *no impact* on the level of U.S. production or exports" and "*little positive impact* on the world price for cotton in the long term;"[50] or (b) that "the effect" of U.S. marketing loan and counter-cyclical payment programs is "present" significant price suppression within the meaning of Article 5(c) and 6.3(c) of the *SCM Agreement*.

A. Brazil's Arguments About the Effects of the Step 2 Program and World Market Price Effects Continue to Shift

35. Although Brazil has argued throughout the original panel proceedings and in this proceeding that allegedly high levels of U.S. exports are the cause of significantly suppressed world market prices[51], Brazil attempts now to change its basic theory of significant price suppression. Indeed, it does so after having attempted to simply dismiss the evidence of declining U.S. exports as a temporary phenomenon that was simply a function of U.S. producers "cleaning out the stocks in their warehouses" prior to the termination of the Step 2 program.[52] In the face of the substantial countervailing evidence, Brazil has been forced to seek a new theory to fit the facts. In its "oral" presentation, Brazil now argues that it is increasing U.S. stocks of upland cotton – not the export of U.S. cotton – that is suppressing world market prices.

36. Brazil has submitted no evidence – or even fully laid out the arguments – to support its 11th hour theory of significant price suppression. And Brazil cannot simply transpose its earlier arguments regarding the effects of exports. While stocks of any commodity are an important factor influencing the world supply and demand balance and, therefore, prices, there is no basis – and Brazil has not provided any – for suggesting that an increase in stocks can have the same impact on world

[49] Bancomext 2005 Annual Report, pp. 2, 26; http://www.bancomext.com/Bancomext/publicasecciones/secciones/7304/AnnualReportBancomext2005.pdf (Exhibit US-134).

[50] Brazil First Written Submission, para. 206 (quoting Brazil First Written Submission, Annex II, paras. 41-43).

[51] *See, e.g.*, Brazil First Written Submission, para. 2.

[52] Brazil Rebuttal Submission, para. 82.

market prices as actual exports. When stocks are held – *i.e.*, are removed from trade on the world market – any possible impact on prices is necessarily substantially less than if they were being traded.

37. Moreover, the price impact of existing U.S. stocks is necessarily greater *within* the United States than it is in the world market. And, consistent with this, U.S. prices have been lower than normal in relation to the A index almost throughout the entire 2006 marketing year.[53] Between August 2001 and July 2005, the A Index averaged 4.69 cents above the nearby NY futures. Since August 2006, the "A" has averaged between 5 and 10 cents above NY futures.[54] As a result of this and other market signals, U.S. producers are reducing plantings. Returns to cotton producers are below expectations and plantings in the United States are expected to decline 14 percent or more in 2007.[55] In short, the evidence concerning the effects of stocks on U.S. prices and the corresponding response of U.S. farmers is *not* consistent with Brazil's new theory that U.S. stocks are suppressing world market prices.

38. This conclusion is reinforced when one considers other factors in the world market. For example, *total* world stocks are expected to decline in 2006 from 2005 levels.[56] Moreover, the world stocks-to-use ratio for cotton has declined for the second year in a row, meaning that the world is using more cotton than is being produced.[57] This is consistent with the fact that world market prices are rising and are expected to continue to do so. While Brazil asserts these prices should be even higher, it has offered no evidence – other than unfounded allegations by its hired economist – to support that assertion.

39. Similarly, the behaviour of other market participants – including Brazil – does not evidence any perception of significant price suppression as a result of U.S. stocks. To the contrary, Brazil and India are expected to increase production in 2007, with recent reports from Brazil anticipating a near-record crop in 2007.[58] By planting and producing more cotton in 2007, India's and Brazil's farmers would appear to be receiving positive signals from current world prices. U.S. production, meanwhile, decreased in 2006, exports are declining in 2006, and U.S. planting is expected to decline substantially in 2007. Again, these are not facts indicative of significant price suppression as a result of U.S. stocks.

40. Thus, Brazil's last minute theory that U.S. *stocks* – not exports – are causing significant price suppression is unsupported by evidence.

B. Brazil's Arguments About the Alleged Effects of the Marketing Loan and Counter-Cyclical Payment Programs Are Misleading, and the Evidence Brazil Submits Actually Confirms the U.S. Position Regarding the Marketing Loan and Counter-Cyclical Payment Program

41. Brazil's "oral" statement seeks to respond to the U.S. observation that Brazil has failed to provide an evidentiary basis for its claims that the marketing loan and counter-cyclical payment programs are presently causing significant price suppression. Brazil asserts that certain allegedly

[53] Daily A-Index and NY Futures Price Data (Exhibit US-135).

[54] Daily A-Index and NY Futures Price Data (Exhibit US-135).

[55] National Cotton Council 2007 Acreage Survey available at http://www.cotton.org/econ/reports/intentions.cfm.

[56] USDA Foreign Agricultural Service, Cotton: World Markets and Trade, February 2007 (available at http://www.fas.usda.gov/currwmt.asp).

[57] USDA Foreign Agricultural Service, Cotton: World Markets and Trade, February 2007 (available at http://www.fas.usda.gov/currwmt.asp).

[58] ICAC Cotton This Month (1 March 2007) (Exhibit US -136).

"key" pieces of evidence support its claims of a breach of Articles 5(c) and 6.3(c) of the *SCM Agreement*.[59] None of this evidence withstands scrutiny, however.

1. None of the Evidence Submitted By Brazil Regarding the Nature, Magnitude and Effects of the Marketing Loan and Counter-Cyclical Payments Indicates That the Payments Are Having Significant Price Suppressive Effects

42. ***Counter-cyclical Payments:*** Brazil's "oral" presentation contains no empirical evidence to support Brazil's claims that counter-cyclical payments are having significant production- or export-inducing effects, or that they are significantly suppressing world market prices. Indeed, Brazil's "empirical evidence" appears to consist of little more than the naked assertion that counter-cyclical payments "restrict planting flexibility," "reduce the risk associated with producing the base crop" "increase the ability of farmers to invest in production-enhancing equipment" and "smooth revenue flow. . . and ease access to credit."[60] While all these things may well be true to some extent, Brazil has not explained why they support a finding that the payments cause significant price suppression. Indeed, almost all of these consequences asserted by Brazil also can be attributed to direct payments and, indeed, to *any* payment to a producer of a crop. The *exact* same planting flexibility restrictions apply in the case of both direct and counter-cyclical payments. Moreover, *any* payment to producers will "increase the ability of farmers to invest in production-enhancing equipment," "smooth revenue flow. . . and ease access to credit."[61] However, those factors did not support any finding of significant price suppression with respect to direct payments in the original proceeding. And, in indeed, the negotiators of the WTO agreement expressly found that Members could provide a whole range of payments to agricultural producers, all of which presumably would have the general effects Brazil attributes to counter-cyclical payments, and yet still have "no, or at most minimal, trade-distorting effects or effects on production."[62]

43. Indeed, from a structural standpoint, Brazil recognizes that the "crucial difference" between the direct and counter-cyclical payments is that the farmer is assured of receiving the former each year but not the latter, because counter-cyclical payments are provided only if the season-average farm price ends up being below the threshold set out in the statute.[63] As the United States has explained in response to questions from the Panel, some analysts have examined whether this difference results in any substantial differences in the *effects* of the two programs, and they have concluded that it likely *does not*.[64] For example, Westcott *et. al.* determined that the link to prices may, in some circumstances, result in indirect production effects stemming primarily from lowered risk of price volatility. However, they concluded that the degree of any such production effects is likely to be minimal and mitigated by a number of factors including that:

(a) where prices are expected to be above maximum threshold – counter-cyclical payments behave just like the fixed direct payments[65];

(b) "cross-commodity effect[s] suggest[] that CCPs may provide a general reduction in revenue risks rather than a crop-specific effect. Net returns among alternative crops would remain the primary consideration underlying production choices;"[66]

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[59] Brazil Oral Statement, para. 25.

[60] Brazil Oral Statement, para. 41.

[61] Brazil Oral Statement, para. 41.

[62] *See* Annex 2 of the *Agreement on Agriculture*.

[63] Brazil Oral Statement, para. 50.

[64] *See* U.S. Answers to Parts D-E of the First Set of Panel Questions, para. 27 (6 March 2007).

[65] Paul A. Westcott, "Counter-Cyclical Payments Under the 2002 Farm Act: Production Effects Likely to be Limited" at 203 (Exhibit US-35).

(c) "while a number of studies indicate that farmers are risk averse (Chavas and Holt, 1990, 1996, for example), other risk reduction instruments already exist to manage risks. Thus, with revenue risk reduction now provided by CCPs as part of farm programs, farmers may adjust their use of these other farm and nonfarm risk management strategies;"[67] and

(d) "a large portion of output in the U.S. agricultural sector is produced by a small share of large producers. . . . Evidence that risk aversion decreases as income rises (Chavas and Holt, 1990, 1996) suggests that risk aversion may also tend to decline as the size of farms increases. Thus, with larger farms that account for most production being less averse to facing risk, this lowers potential production effects of CCPs due to risk reduction. And while smaller farms may be more risk averse in their farm enterprise, off-farm income may reduce the overall level of household income risk."[68]

44. Studies looking to the actual effects of counter-cyclical payments confirm their minimal impacts on planted acreage and production. For example, as the United States has explained, a 2007 study by Lin & Dismukes found that "[t]he effect of CCPs on producers' planting decisions . . . appears to be *very negligible* – an increase in the acreage of major field crops of less than 1% ... ."[69] The United States has submitted this and other studies examining the empirical evidence regarding the actual effects of counter-cyclical payments on corn, wheat, and soybean producers in recent years, including MY 2005, the marketing year on which Brazil has placed special emphasis. The United States also has provided studies taking a more qualitative assessment of the question at hand.[70] These studies support a finding that counter-cyclical payments have – at best – minimal effects on plantings and production (and, thus, are likely to have negligible effects on world market prices).

45. In its unsolicited third written submission – BRA-659 – Brazil asks the Panel simply to disregard all of these studies.[71] For the reasons discussed above, Brazil's submission was made in breach of the Panel's working procedures and is not properly part of the record before the Panel. Nonetheless, the United States would make the following points as to why the arguments made by Brazil therein are unavailing. Brazil complains that the studies do not relate specifically to counter-cyclical payments made in respect of upland cotton. However, as the United States has explained, there is no reason why that should preclude the Panel from considering the studies as being highly relevant.[72] Indeed, Brazil has not submitted any evidence – save for the unsupported assertions of its

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[66] Paul A. Westcott, "Counter-Cyclical Payments Under the 2002 Farm Act: Production Effects Likely to be Limited" at 204 (Exhibit US-35).

[67] Paul A. Westcott, "Counter-Cyclical Payments Under the 2002 Farm Act: Production Effects Likely to be Limited" at 204 (Exhibit US-35).

[68] Paul A. Westcott, "Counter-Cyclical Payments Under the 2002 Farm Act: Production Effects Likely to be Limited" at 204 (Exhibit US-35).

[69] Lin, William and Dismukes, Robert. "Supply Response Under Risk: Implications for Counter-cyclical Payments' Production Impacts," *Review of Agricultural Economics–Volume 29, Number 1–Pages 64-86*, forthcoming, p. 83 (Exhibit US-85) (emphasis added).

[70] U.S. Rebuttal Submission, para. 226-252.

[71] Supplementary Statement of Daniel Sumner, paras. 18-38.

[72] Brazil also makes the inexplicable argument that a number of the studies submitted by the United States are not relevant because they allegedly do "not examine whether CCPs are decoupled from production. Rather, [they] examine whether CCPs increase acreage." Supplementary Statement of Daniel Sumner, para. 21. Brazil applies this criticism, for example, to the 2007 study by Lin & Dismukes finding "very negligible" increases in the acreage of major field crops. Brazil appears to be confused about its own claims and arguments in this proceeding. As the United States understands it, Brazil's claim here is that marketing loan and counter-cyclical payments are presently significantly suppressing world market prices. Brazil's theory to support this claim has been that these payments affect the planting decision, causing U.S. producers to plant more than they otherwise would and that this ultimately leads to oversupply and suppressed world market prices. It is remarkable, therefore, that Brazil would attempt to *dismiss* studies because they look at effects of payments on

hired economist – to show that the effects would be substantially different in the case of upland cotton, especially given that *no base acre holder has to produce anything, let alone the base crop, in order to receive any payments under the program*. More importantly, Brazil appears to forget that *it is Brazil that bears the burden of proving its claims in this proceeding.* Indeed, while Brazil insists that only cotton-specific studies may be considered as relevant, Brazil has not itself provided *a single* study that examines the actual effects of counter-cyclical payments made specifically in respect of upland cotton production. Moreover, what studies Brazil has provided do not detract from the substantial evidence showing that – as a matter of fact – counter-cyclical payments have minimal acreage and production effects.[73] Therefore, Brazil's allegations of significant planting effects are just that – allegations. They are supported neither by the empirical evidence nor any studies conducted in light of such evidence.

46. Brazil has no answer either to the studies finding that a substantial part of counter-cyclical payments are capitalized into land values and land rents. Although Brazil argues that the Panel should simply disregard this evidence, Brazil has not explained why the following conclusion of the OECD is not valid and entirely relevant to the question at hand:

> Empirical work suggests that PFC and MLA payments had a significant effect on land values and rental rates. Given the importance of the rental market for land in the United States, it appears that *there was a relatively high "pass-through" of the additional income generated by the payments to landowners, many of whom are not the actual operators of the land*. It appears that the payments primarily had the effect of increasing the value of the principal fixed asset in agriculture—land.[74]

47. Indeed, the United States recalls that Brazil has argued that the more certainty there is about whether payments will be received, the more likely they are to be capitalized into land values and

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acreage and suggest that what is relevant is some undefined inquiry into whether payments are "coupled" to production (an inquiry, incidentally, that has no basis in the text of Articles 5(c) and 6.3(c)).

[73] Indeed, the study that Brazil has touted as "more recent and more relevant" than the numerous studies submitted by the United States does not even examine the behaviour of actual farmers – let alone upland cotton farmers. *See* McIntosh, Christopher R, Jason F. Shogren and Erik Dohlman,"Supply Response to Counter-Cyclical Payments and Base Updating under Uncertainty: An Experimental Study,: forthcoming paper in the *American Journal of Agricultural Economics*, November 2006, page 18 (Exhibit BRA-565). Rather, it looks to the results of a laboratory experiment conducted using University students as "laboratory decision-makers." Brazil criticizes the United States for allegedly "attempt[ing] to discredit research findings in economics simply because they derive from controlled experiments." Supplementary Statement of Daniel Sumner, para. 38. According to Brazil, this is "30 years out of date." Supplementary Statement of Daniel Sumner, para. 38. However, Brazil makes no effort to reconcile this view with its own arguments that U.S. studies should be dismissed if they do not examine the precise acreage responses of *upland cotton* farmers. Nor does Brazil address the fundamental limitations noted by authors themselves in respect of the laboratory experiment. *See* McIntosh, Christopher R, Jason F. Shogren and Erik Dohlman,"Supply Response to Counter-Cyclical Payments and Base Updating under Uncertainty: An Experimental Study,: forthcoming paper in the *American Journal of Agricultural Economics*, November 2006, page 18 (Exhibit BRA-565) ("Our design did not address two features of the 2002 Act which could affect the interpretation of our results. First, there are no adjustments made in our bonuses for the fact that direct and counter-cyclical payments are made only on a percentage (85 percent) of base acres. If these adjustments were incorporated, the lump sum bonuses would have been lower, implying our results could overstate the effects of CCPs. Second, we excluded the marketing loan program to focus on the basic CCP structure—target price, market price, and direct rate. Adding the marketing loan program into our design would temper the basic effects of CCPs by providing an additional price support mechanism.")

[74] Abler, David, and David Blandford. A Review Of Empirical Studies Of The Acreage And Production Response To US Production Flexibility Contract Payments Under The Fair Act And Related Payments Under Supplementary Legislation, Directorate For Food, Agriculture And Fisheries Committee For Agriculture, OECD, Paris, AGR/CA/APM(2004)21/FINAL, p.17 (25 March 2005) (Exhibit US-32) (emphasis added).

rents.[75] Given that MLA payments were provided as part of *ad hoc* legislation – unlike counter-cyclical payments which have been established well ahead of time as a part of the FSRI Act of 2002 – farmers were presumably even less likely to have anticipated MLA payments than counter-cyclical payments. Thus, the degree of capitalization into land values and rents is presumably even *greater* than that found in the OECD study for MLA payments. And, as the OECD study concluded:

> If PFC and MLA payments were captured largely by landowners through higher land values and land rents, then the scope for these payments to influence agricultural production would be narrowed. Farmers renting land would not be able to use payments associated with their rented land to cover fixed or variable costs. These farmers would be no more able to secure capital from traditional lenders than in the absence of the payments. They would see no increase in wealth, at least on the land that they rent, ruling out a risk-related wealth effect. Expectations of future payments associated with rented land would not affect decisions by renters because they would not capture these payments. The payments would not affect a renter's decision to remain in or to exit from agriculture, although they could affect a landlord's decision to keep land in agriculture.[76]

48. Brazil's only response to this evidence is that it is "mathematically impossible" that direct and counter-cyclical payments "are capitalized into land rents and captured by the land owner."[77] Brazil has not explained why – if this were so – the OECD could have come to such a fatally flawed conclusion (especially given that the OECD conclusions cited above were actually reached after reviewing a *number* of different studies all examining the pass-through effects of PFC and MLA payments).

49. In fact, the flaw is in the data that Brazil uses to allege its "mathematical impossibility." As the United States explained in its rebuttal submission, instead of examining actual land rents – as Brazil purports to do – Brazil actually considers an *imputed* economic cost to land that the USDA calculates by valuing the alternative uses of the asset (for example, renting it to another producer).[78] To make matters worse, Brazil looks at average imputed rental values for land on farms *with* payment base acres and *without* payments base acres, despite the fact that the former would have a substantially higher rental value precisely *because* of the payments associated with them. Brazil's response that *different* levels of payments are made on different base acres because of differences in historical yields misses the point entirely, and is no justification for comparing farmland linked to payment base with farmland *not* linked to payment base acres as Brazil attempts to do.

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[75] Brazil Rebuttal Submission, para. 146.

[76] Abler, David, and David Blandford. A Review Of Empirical Studies Of The Acreage And Production Response To US Production Flexibility Contract Payments Under The Fair Act And Related Payments Under Supplementary Legislation, Directorate For Food, Agriculture And Fisheries Committee For Agriculture, OECD, Paris, AGR/CA/APM(2004)21/FINAL, p.17 (25 March 2005) (Exhibit US-32).

[77] Brazil Oral Statement, para. 46.

[78] U.S. Rebuttal Submission, para. 259.

50. While it is sparse, it is also instructive to consider the type of evidence that Brazil actually *does* rely upon to support its claims regarding counter-cyclical payments. Brazil invokes as evidence of "present" significant price suppression resulting from counter-cyclical payments, a statement made *in February 2001 – i.e.,* before either the 2002 FSRI Act or the counter-cyclical payments authorized thereunder went into effect – by a National Cotton Council representative about *emergency relief provided under the FAIR Act of 1996* as to whether that relief helped cotton farmers "avoid bankruptcy" in the period MY 1999-2001.[79] This statement – quoted out of context – about emergency relief under the FAIR Act of 1996 including production flexibility contract payments, marketing loss assistance payments, and disaster payments, offers no insight regarding the role of counter-cyclical payments in production decisions or about U.S. farmers' costs and revenues today. Certainly it does nothing to detract from the actual data regarding "present" costs and revenue, which, as discussed below, flatly contradict Brazil's claims that U.S. upland cotton farmers would be bankrupt without the marketing loan and counter-cyclical payment programs. In fact, while this "evidence" makes no substantive contribution to the issues before the Panel, the fact that this is the type and quality of "empirical evidence" upon which Brazil must rely speaks volumes about the lack of an evidentiary basis for Brazil's claims.

51. ***Marketing Loan Payments:*** Brazil's arguments regarding marketing loan payments are no more availing than its arguments about the counter-cyclical payments. Indeed, rather than providing actual evidence regarding the effects of the marketing loan payments, Brazil attempts to simply sidestep the issue by, again, (a) asserting that the matter has already been resolved by the original panel while at the same time (b) mischaracterizing the U.S. arguments to avoid engaging on the real issues at hand. Brazil's approach lacks merit.

52. First, the United States reiterates that the question of whether or not marketing loan payments are causing "present" significant price suppression today was not considered by the original panel. To the contrary, that panel expressly declined to consider the effects of any future payments allegedly "mandated" to be made under the Step 2, marketing loan, and counter-cyclical payment programs. The original panel also declined to consider whether the marketing loan and counter-cyclical payment *programs* would necessarily have adverse effects in the future; a finding that – by Brazil's own admission – would have been *required* for the original panel to have made a finding against the programs as such.[80] Moreover, as Brazil has conceded, the market conditions that existed at the time of the original proceeding are very different from those that prevail at present.[81]

53. Indeed, the market conditions are even more different now than Brazil cares to admit. The Step 2 program is no longer in effect, and since the termination of the program, U.S. exports in

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[79] Brazil Oral Statement, para. 43.

[80] For example, in the case of its claims against the challenged programs, *per se*, Brazil asked the Panel "to find that the mandatory provisions of the 2002 FSRI Act and the 2000 ARP Act together with their implementing regulations, as listed above, *cannot be applied in a WTO consistent manner*." Brazil's 9 September 2003 Further Submission, para. 435-436. Explaining what this would mean in the context of this dispute, Brazil argued "[f]irst, the Panel needs to evaluate whether the U.S. subsidies will *necessarily threaten* to cause serious prejudice at price levels below the trigger prices of the U.S. subsidies. Second, the Panel needs to consider whether the U.S. subsidies threaten to cause serious prejudice *even at price levels at which only crop insurance subsidies and direct payments are made*." Brazil's 9 September 2003 Further Submission, para. 426 (emphasis added). The original panel did not conduct the requested evaluation and did not make the requested findings.

[81] *See* Brazil Rebuttal Submission, paras. 235-236 (In an effort to excuse itself from having even to show any *coincidence* of U.S. payments and price suppression, Brazil argued that "the underlying statutory and regulatory bases for U.S. upland cotton subsidies and market conditions provided the original panel with a fairly dynamic environment in which to examine temporal coincidences. The period MY 2001-2005 (principally under the FSRI Act of 2002) was more stable. After MY 2001, it did not involve the same extreme declines in the world market prices for upland cotton or significant additional increases in the U.S. share of world production and exports, compared to the period MY 1998-2002.")

MY 2006 are sharply lower than in recent years. U.S. exports for MY 2006 are *down 30 percent* from the levels observed at the same time last year.[82] Weekly cotton sales are *31 percent below* the 5-year average.[83] And total U.S. export commitments are currently approximately *40 percent below* last year's level and *27 percent* below the 5-year average.[84] Forecasts for the future are similarly gloomy. As the United States explained in the panel meeting, in February, USDA lowered the U.S. cotton export forecast for MY 2006 by nearly 8 per cent, following a 2 percent downward revision in January.[85] These downward revisions are taking place at the same time that USDA estimates record *high* foreign cotton mill use, which means that U.S. share of foreign consumption is expected to drop from 16 percent in MY 2005 to 12 percent in MY 2006. Moreover, U.S. share of world exports is expected to drop from 40 percent in MY 2005 to 36 percent in MY 2006. U.S. domestic mill use for MY 2006 is projected at just 5 million bales, the lowest since MY 1931. The declining demand for U.S. upland cotton is also being reflected in planting and production decisions. The annual survey of planting intentions conducted by the National Cotton Council indicates that U.S. upland cotton plantings are likely to be down an average of 14 percent in MY 2007 from 2006 levels.[86]

54. To the extent that Brazil asserts that the original panel already examined and resolved the question of what effects the marketing loan has under such market circumstances as prevail now, the United States submits that Brazil's argument is wholly without merit.

55. Second, it is astonishing that Brazil yet again asserts that "the United States never explains how marketing loan subsidies could have no effect on producers' decision to plant cotton ... ."[87] Not only has the United States never *alleged* that " marketing loan subsidies could have no effect on producers' decision to plant cotton,"[88] but the United States and Brazil's own economist appear to agree on precisely the conditions under which marketing loan payments might affect producers' decision to plant cotton. Specifically, to determine whether marketing loan payments have effects in any given year, it is necessary to examine the planting decisions made by U.S. producers in light of the conditions as they existed as of the time of planting for each marketing year (i.e., January-March).[89] A producer's expectations at that time about market revenue and/or revenue from government payments, costs and other factors will determine whether cotton or some other crop is planted, or if the land is put to other use. Brazil conceded this point both in this proceeding[90], and in the original proceeding.[91]

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[82] Weekly Export Performance Report for week ending February 15, 2007 (Exhibit US-113).

[83] Weekly Export Performance Report for week ending February 15, 2007 (Exhibit US-113).

[84] Weekly Export Performance Report for week ending February 15, 2007 (Exhibit US-113).

[85] February 2007 World Agricultural Supply and Demand Estimates (WASDE) Report (Exhibit US-114).

[86] National Cotton Council Planting Intentions Survey MY 2007 (Exhibit US-115).

[87] Brazil Oral Statement, para. 35.

[88] This is the second time that the United States has addressed the same mischaracterization of the U.S. position. *See e.g.*, U.S. Rebuttal Submission, para. 268 ("Brazil's rebuttal arguments about the structure, design, and operation of the marketing loan program are, yet again, premised on a mischaracterization of the U.S. arguments. Brazil asserts that 'the United States argues that upland cotton producers do not expect to receive marketing loan payments. . . .The United States argues that marketing loan payments . . . have no effect on planted acreage, no effect on production, no effect on exports, and no effect on the world price of cotton.' Brazil Rebuttal Submission, para.101. This is not what the United States has argued and the United States respectfully refers the Panel to the U.S. first written submission at paragraphs 203-225 where the actual U.S. arguments are set out in detail.")

[89] *See e.g.*, Cotton Percent Planted, 15 Selected States (Exhibit US-44).

[90] *See* Brazil First Written Submission, Annex I, para. 36 ("U.S. cotton producers respond to the *expected* prices and *expected* rates of subsidy that apply at the time planting and other key decisions are made in the production cycle") (emphasis added) and Brazil First Written Submission, Annex I, para. 58 ("[t]he magnitude of the impact on incentives to produce cotton is equal to the *expected* difference between the loan rate, which is known at planting time, and the grower's *expectations* at the time of planting about the AWP for

56. Nonetheless, while Brazil agrees with the United States as to the correct analysis, Brazil continues to present evidence that directly contradicts this analysis. For example, in its "oral" presentation, Brazil alleges that marketing loan payments in MY 2005 were 29 percent higher than in MY 2002 and, according to Brazil, this "*alone* strongly suggests that its effects on U.S. production and exports as well as on world market prices are much greater [than in the period before the original panel]."[92] Yet Brazil concedes that the *effects* of the marketing loan payments are a function of expectations regarding payments, not actual payments received. Indeed, in its modeling exercise purporting to examine the effects of marketing loans, Brazil's economist does not even include actual payments, explaining:

> U.S. producers respond to revenue they expect to receive from market prices and expected government subsidies, where relevant expectations are those that are held around the time that planting and other key production decisions are made. U.S. producers do not know with certainty what actual prices and subsidies will turn out to be as they unfold during the marketing year. *Therefore, as in reality, the model assumes that actual prices or subsidies in a marketing year do not affect cotton growers' behaviour in that marketing year*.[93]

57. It is telling that Brazil repeatedly misstates the U.S. position and continues to offer evidence that is fundamentally at odds with the correct analysis of possible price effects (which it has expressly acknowledged). The fact is that Brazil has not – indeed, cannot – show that U.S. cotton producers' expectations regarding marketing loan payments in have actually led to "present" significant shifts in planting. Indeed, as discussed next, the data submitted by Brazil regarding producers' expected revenues and costs show that producing upland cotton was both economically viable and rational in every year under the FSRI Act, including MY 2006 (the relevant year for purposes of Brazil's "present" serious prejudice claims).

2. The Cost of Production Analysis Submitted By Brazil Is Fundamentally Flawed and the Proper Assessment of the Data Supports the U.S. Argument That Marketing Loan and Counter-Cyclical Payments Are Not Having Any Significant Price Suppressive Effects

58. The centerpiece of Brazil's oral presentation regarding serious prejudice is a series of six charts[94] and accompanying discussion that Brazil presents to show the allegedly "economically irrational business of growing cotton in the United States within marketing loan and CCP subsidies."[95] Brazil submits that this evidence establishes that U.S. upland cotton producers would not plant upland cotton and could not survive without marketing loan and counter-cyclical payments. As the United States shows below, however, Brazil's analysis is inconsistent with the economic literature regarding the role of costs in planting decisions, the findings of the Appellate Body regarding the relevance of variable versus total costs, and the approach taken in all econometric models of which the United States is aware that look to costs as a factor in planting decisions (including Brazil's own model in the original proceeding). Indeed, viewed consistently with the principles recognized therein, the data show that (a) upland cotton producers expected and were able to meet their variable costs in every

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cotton that will apply when the grower makes that marketing loan transaction.") (emphasis added). Brazil Further Submission, Annex I, para. 17-18.

[91] *US – Upland Cotton (AB)*, para. 440 ("Brazil counters that farmers decide what to plant based on expected market prices as well as expected payments under the challenged subsidy programs, such that planted acreage responds to both these factors.")

[92] Brazil Oral Statement, para. 31.

[93] Brazil First Written Submission, Annex I, para. 4 (emphasis added).

[94] In fact, there are only three charts, with a second associated chart for each that isolates one of the columns therein.

[95] Brazil Oral Statement, para. 57 and paras. 57-91.

year under the FSRI Act solely with market revenue; (b) that upland cotton was the most attractive crop from a cost/revenue perspective in most years; (c) upland cotton producers met and exceeded even their *total* cash costs in almost every year under the FSRI Act of 2002.

59. What Brazil's analysis lays bare is not the "economically irrational business of growing cotton in the United States within marketing loan and CCP subsidies,"[96] as Brazil alleges, but rather the distortive and unfounded nature of Brazil's cost analysis.

a. Variable costs – not total costs – are the relevant measure in assessing year-to-year planting decisions

60. It is useful to begin with a summary of what Brazil purports to show. Specifically, Brazil asserts that it is providing: (a) a chart showing expected market revenue net of total costs of production for corn, soybeans, and cotton in MY 2005; (b) a chart showing expected market revenue net of total costs of production for corn, soybeans, and cotton in MY 2007; and (c) a chart showing average market revenue net of total costs of production for corn, soybeans, and cotton in MY 2002-2006. Brazil argues that in each of these time periods, U.S. farmers would have lost money *across the board* producing *any* of these crops (or would have expected to do so) "but for" marketing loan and counter-cyclical payments. According to Brazil, this analysis shows that U.S. farmers producing cotton, soybeans, or corn can only survive because of those payments. Brazil further alleges that it is only when those payments are taken into account that *upland cotton* becomes an attractive crop relative to the others. Brazil is wrong.

61. Even before addressing the numerous technical flaws in Brazil's analysis, it is useful to put Brazil's argument in perspective; in particular, the remarkable assertion that U.S. farmers could not produce *soybeans*, *corn*, or *cotton* in the United States in any of the periods examined absent marketing loan and counter-cyclical payments. Indeed, although the United States has almost one billion acres of farmland, and although corn and soybeans were two of the top five top agricultural commodities in MY 2005, Brazil would have the Panel believe that producing those crops and cotton – indeed, perhaps even agriculture itself – is an ""economically irrational business" in the United States. This premise is simply untenable. In fact, it demonstrates precisely the flaws in the analysis presented by Brazil – that ***total costs in each year are <u>not</u> the proper considerations in assessing the viability of farmer's year-to-year planting decisions***.

62. Rather, for a farmer, the relevant costs in deciding what to plant in each year are variable costs of production. Recall the simplified example examined in the first U.S. submission of a farmer deciding in January of a particular year whether to plant all soybeans, some soybeans and some cotton, all cotton, or to allow the land to sit idle. This farmer will consider, *inter alia*, the expected price of cotton at harvest, the expected price of soybeans at harvest, as well as the anticipated costs of growing each crop. In so doing, he does not need to consider fixed asset and overhead costs. He has already incurred those costs; they will not differ based on whether the farmer plants soybeans, cotton, a mix, or nothing. Rather, the farmer will consider projected net revenues taking into account costs for such items as seed, fertilizer, chemicals, and other expenses that are directly related to planting, harvesting, and marketing each crop. The economically rational decision for him will be to plant the crop, or mix of crops, that *both* covers his variable costs *and* maximizes his net revenue. In other words, the farmer will choose the option that gives him the largest margin above variable costs. This will not only allow him to cover his variable expenses but will also give him the most revenue to pay down total costs.

63. That variable costs are the relevant consideration in year-to-year planting decisions is well-accepted in agricultural economics. The United States discussed the extensive literature in this regard

[96] Brazil Oral Statement, para. 57 and paras. 57-91.

in its submissions to the panel in the original proceeding.[97] To supplement that discussion, the United States submits two other studies that confirm that variable costs are the appropriate consideration in assessing year-to-year planting decisions.[98] Considering the evidence submitted earlier in the dispute, the Appellate Body expressly recognized that:

> We agree with the general proposition of the United States that *variable costs may play a role in farmers' decision-making as to whether to plant upland cotton or some alternative crop, and how much of each crop to plant*. From a short-term perspective, variable costs may be *particularly important*.[99]

64. Moreover, the fact that variable costs – not total costs – is the appropriate measure is also evidenced by the fact that there is *no economic model* of which the United States is aware that uses total costs in its supply response equations (that is, to examine the planting decision). Indeed, FAPRI uses variable costs in its modeling framework. And even Brazil's model in the original proceeding – purportedly based on the FAPRI model – used variable costs in the net revenue equation that determined the planting decision of farmers.

65. Thus, there is no basis whatsoever for Brazil's use of total costs to examine planting decisions in any particular year.

b. U.S. farmers expected to meet and exceed variable costs in each year, and in most years upland cotton was the most attractive option

66. When a proper examination is undertaken regarding the expected returns and variable costs, the data show that U.S. farmers expected to cover their variable costs regardless of whether they decided to grown cotton, corn, or soybeans. Brazil has acknowledged that if a "farmer would not be able to cover even variable costs, he or she would not plant anything at all to minimize losses."[100] Conversely, where, as here, the farmer *is* covering his variable costs, it is economically rational for him to plant *something*. The question is then *what* to plant. On that question, the assessment depends on a number of factors including the relative net revenue, considerations of weather, and considerations of other factors affecting yields (such as pests and disease). As shown below, in most years, upland cotton was the most attractive option from the standpoint of costs and revenues.

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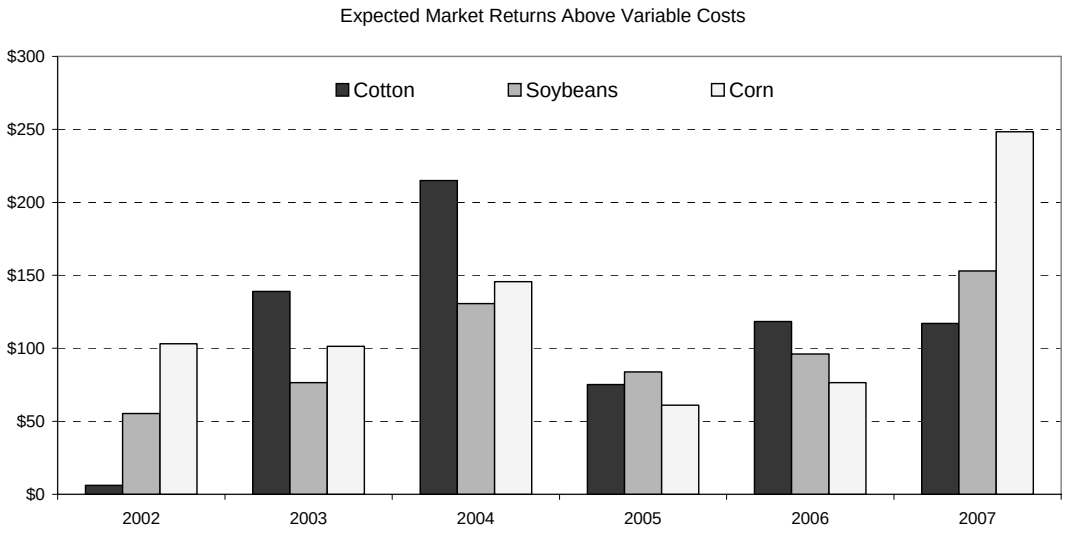
[97] *See e.g.*, U.S. Further Rebuttal Submission in the Original Proceeding, paras. 117-122 (18 November 2003).

[98] *See* Cecil Davison and Brad Crowder, "Northeast Soybean Acreage Response Using Expected Net Returns" *Northeastern Journal of Agriculture and Resource Economics*, April 1991, pp. 33-41 (Exhibit US-137) and Duncan M. Chembezi and Abner W. Womack, "Regional Acreage Response for U.S. Corn and Wheat: The Effects of Government Programs", *Southern Journal of Agricultural Economics*, July 1992, pp 187-198 (Exhibit US-138).

[99] *US – Upland Cotton (AB)*, para. 453.

[100] Brazil Oral Statement, para. 67.



67. The U.S. analysis above seeks to replicate the revenue expected and variable costs faced by actual U.S. cotton farmers. Each aspect of the calculation is described in Annex I.[101] As discussed therein, the United States has examined relative costs and revenue of growing upland cotton, corn, and soybeans in the 17 U.S. cotton-producing states.[102]

68. The analysis shows that for the entire period MY 2002-2007, U.S. cotton farmers expected to meet or exceed their variable costs of planting cotton, corn, *or* soybeans. Therefore, it was economically rational for those farmers to plant *something*, rather than leaving the land idle. In terms of *what* to plant, upland cotton was the most attractive option – from the standpoint of costs and revenue – in at least three of the years (MY 2003, MY 2004, and MY 2006). In MY 2002, 2005, and 2007, cotton was not the most attractive option. It is instructive to examine more closely shifts in upland cotton acreage in those years because that shows precisely that, contrary to Brazil's assertions, U.S. farmers' planting decisions correspond to market signals.

69. In MY 2002, upland cotton was least attractive of the three options, and U.S. planted acreage declined correspondingly from 15.5 million acres in MY 2001 to 13.7 million acres in MY 2002.

70. In MY 2005, soybeans appeared to be the most attractive crop, followed by cotton. In this circumstance, the expectation was that cotton acreage would fall slightly. In fact, however, it increased slightly – by approximately 600,000 acres. What explains this increase? Brazil has attempted repeatedly to attribute this to the alleged effects of marketing loans and counter-cyclical payments. However, the data point fairly precisely to the reason for the slight increase in cotton acreage in MY 2005 – a shift away from soybean acreage due to concerns about an outbreak of Asian soybean rust at the end of MY 2004. Soybean rust, a recurrent problem for soybean producers in much of the southern hemisphere, was first detected in the United States in the Fall of 2004, late enough in the season that it posed no threat to that year's soybean crop. After overwintering in the South, soybean rust posed a new, uncertain, and potentially large threat at the beginning of the 2005

[101] The back-up data is also provided in Exhibit US-139.

[102] In other states, cotton does is not a competitor crop and, therefore, corn and soybean costs from those states would distort the picture.

U.S. soybean season.[103] Soybean rust has been detected in eight states in the Delta and Southeast regions since late 2004.[104] It was in these regions that the shift from soybean acreage to upland cotton acreage occurred in MY 2005. Of the 600,000 acre increase from MY 2004 to MY 2005, almost the entire shift occurred in the Delta region, where an *increase* in 530,000 acres of cotton was offset precisely by a *decrease* of 530,000 acres of soybeans. Thus, it was soybean rust, and not marketing loan or counter-cyclical payments, that was responsible for increased acreage in MY 2005.

Changes in planted acreage, 2004 to 2005

State/ Region	Cotton		Soybeans	
	Change in acres	*% change*	*Change in acres*	*% change*
DELTA	530	15.6	-530	-4.4
Arkansas	140	15.4	-170	-5.3
Louisiana	110	22.0	-220	-20.0
Mississippi	110	10.0	-60	-3.6
Missouri	60	15.8	0	0
Tennessee	110	20.6	-80	-6.6
SOUTHEAST	74	2.5	-330	-10.6
Alabama	0	0	-60	-28.6
Florida	-3	-3.3	-10	-52.6
Georgia	-70	-5.4	-100	-35.7
North Carolina	85	11.6	-40	-2.6
South Carolina	51	23.7	-110	-20.3
Virginia	11	13.4	-110	-1.9
SOUTHWEST	94	1.5	75	2.2
Kansas	-11	-12.9	100	3.6
Oklahoma	50	2.2	5	1.6
Texas	100	1.7	-30	-10.3

Source: *Crop Production*, October 2006, Agricultural Statistics Board, NASS, USDA.

71. In MY 2007, corn is expected to provide greater net revenue than either cotton or soybeans. Cotton acreage is shifting consistent with these, and other, market signals. As the United States noted in the meeting with the Panel, the annual survey of planting intentions conducted by the National Cotton Council indicates that U.S. upland cotton plantings are likely to be down an average of 14 percent in MY 2007 from 2006 levels.[105] While Brazil attempts to dismiss this data – arguing that acreage shifts should be *even* higher – it provides no basis for this assertion. Indeed, a 14 percent shift in acreage would be substantial, amounting to more than a 2 million acre drop in planted acreage and

[103] The Value of Plant Disease Early-Warning Systems: A Case Study of USDA's Soybean Rust Coordinated Framework/ERR-18. Econ. Res. Ser., USDA., pg. 1. http://www.ers.usda.gov/publications/err18/err18.pdf

[104] As of October 3, 2006, National Soybean Rust Commentary, South Carolina officials reported a new county with soybean rust, Saluda County. Soybean rust was found in Washington and Sampson Counties in North Carolina on soybeans. Currently rust has been found infecting this year's soybeans in 68 different counties in eight states: AL, FL, GA, LA, MS, SC, TX, and NC. Including reports on kudzu, there are a total of 88 counties in eight states with rust this year, including 7 in Alabama; 15 in Florida; 18 in Louisiana and South Carolina; 13 in Georgia; 3 in Texas; 2 in Mississippi; and 12 in North Carolina. http://www.sbrusa.net/

[105] National Cotton Council Planting Intentions Survey MY 2007 (Exhibit US-115).

– applying MY 2006 yields – a 3.7 million bale decline in production.[106] Brazil has not explained why this Panel should ignore this important evidence.

72. In any event, what the data show is quite different from what Brazil has asserted about the allegedly "economically irrational business of growing cotton in the United States within marketing loan and CCP subsidies."[107] Even without considering those payments, it is clear that U.S. farmers can – and do – meet their variable costs of production. Moreover, under the circumstances, upland cotton is often the most economically rational choice among the available competing crops. Where it has not been, declines in acreage have ordinarily resulted.

c. U.S. farmers actually met and exceeded variable costs and even total cash costs in most years under the FSRI Act of 2002

73. Finally, the United States recalls that total costs may be a relevant consideration in more long-term decisions such as whether or not to exit farming altogether (*i.e.*, not year-to-year planting decisions).[108] However, Brazil's consideration of total costs of growing upland cotton suffers from a number of flaws.

74. First, Brazil considers total costs of growing upland cotton as the *only* consideration for a farmer in deciding whether to continue to exit farming altogether. This is not accurate. Indeed, as the economic literature confirms, whole-farm costs and revenues – including off-farm revenue and revenue from other sources – are also important considerations in making those kinds of decisions.[109] Brazil's attempts to show that U.S. producers would have exited upland cotton production in the long-term solely on the basis of a comparison of costs and revenues for cotton are, thus, not sound. Brazil has never been able to submit any literature, study, report, or empirical evidence to contradict the evidence submitted by the United States regarding the consideration of whole-farm costs and revenues. Nor has Brazil provided any evidence that takes into account whole-farm costs and revenues, and that shows that, absent the marketing loan and counter-cyclical payment programs, U.S. upland cotton producers would have exited upland cotton farming.

75. Second, Brazil includes in its assessment imputed opportunity costs. These are not actual expenditures, but instead are an economic concept used to capture the alternative uses of the land, unpaid family labour and capital; for example, how much a farmer would pay himself for his own labour. These are not like year-to-year cash costs without which a farmer would be unable to continue on in business. It is only through the inclusion of such imputed costs that Brazil seeks to show returns less than total costs.

76. **The fact is that even if one includes additional fixed cash costs, which are not part of variable costs, the outcome remains much the same as for variable costs; that is, in most years the market revenues from cotton cover variable plus fixed cash costs.** As shown below, in most years, U.S. farmers are able to meet and exceed their *total* cash costs. Therefore, Brazil's claims of

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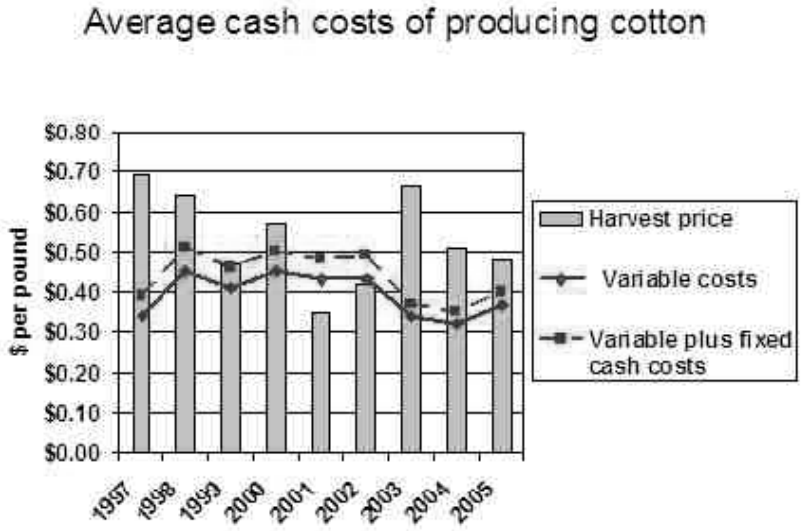
[106] February 2007 World Agricultural Supply and Demand Estimates (WASDE) Report (Exhibit US-114).

[107] Brazil Oral Statement, para. 57 and paras. 57-91.

[108] U.S. First Written Submission, paras. 295-297.

[109] *See e.g.*, Hoppe, Robert A. and Korb, Penni. Understanding U.S. Farm Exits. Economic Research Report 21. June 2006, p. 20 (Exhibit US-46) ("Off-farm work has become important to farm operators. About one-third of farmers have worked off the farm at least 200 days per year—essentially full-time—since 1978. Off-farm work could hypothetically affect exits in two ways. First, off-farm work may be the first step in an exit from farming, which would be reflected in higher exits for farms the operators of which work off-farm. Second, off-farm work might lower the probability of exit by providing farm operator households with another source of income.")

widespread bankruptcies in the absence of marketing loan and counter-cyclical payments are not realistic.[110]



77. Moreover, Brazil has claimed on several occasions that a large cost-revenue gap exists for U.S. cotton producers, such that except for U.S. subsidies, farmers would not plant cotton. Examining the cost data properly for the period 2000-2005, instead of the cumulative $663 *deficit* per acre asserted by Brazil, the cumulative returns over the same period were a *positive* return of $161 per acre. Moreover, for MY 2000-2006, instead of the $837 *deficit* per acre alleged by Brazil, the cumulative net returns were a positive $133 per acre.

d. Conclusion

78. Notwithstanding Brazil attempts to skew the cost data, that data show clearly that U.S. producers actually meet – and, in fact, exceed – their variable costs of producing upland cotton. Moreover, in most years, a relative consideration of variable costs and expected returns shows upland cotton to be the most attractive among competing crops. Where it is not, U.S. farmers behave in exactly the way they would be expected to behave given the particular market signals – they pull back on production except where other considerations (for example, concerns regarding weather, pests or disease) suggest a different approach.

3. The Sumner II Model Is Oversimplified and Relies on Arbitrary Parameters and Assumptions That Have No Basis in the Economic Literature

79. The third piece of allegedly "key evidence" referenced by Brazil in support of its claims of present significant price suppression are the results of the Sumner II model that Brazil commissioned for purposes of this proceeding. As the United States has explained, that model suffers from substantial flaws, both in its structure and operation and in the parameters and assumptions used therein.[111] As a result, the model is overly simplified and produces grossly biased results.

[110] The United States notes that this chart and the back-up spreadsheets were submitted to the Panel and Brazil during the meeting with the Panel. *See* Exhibit US-124.

[111] *See e.g.*, U.S. First Written Submission, Annex I and U.S. Rebuttal Submission, Annex I.

80. Indeed, despite Brazil's efforts to explain it away, Dr. Sumner's own critical assessment of the model – made outside this proceeding – stands. "The simple model" laid out in the 2005 CATO paper – which is virtually identical to the one Brazil has presented in this proceeding – "does not represent the depth of analysis that would be appropriate to support a trade remedy proceeding or a serious prejudice claim before a WTO panel."[112] As Dr. Sumner acknowledged, much of the fault lies with the oversimplifications in the model itself, which "abstract from many complexities that would be important to get more precise estimates."[113] Unfortunately, Dr. Sumner substantially compounded these flaws through his deliberate selection of modeling assumptions and parameters that exaggerate any possible effects of the counter-cyclical and marketing loan programs. As the United States demonstrated at the meeting with the Panel and as shown in the table below, between the original panel proceeding and this Article 21.5 panel proceeding, Dr. Sumner *changed every single elasticity estimate in his modeling exercise, except one* (U.S. mill demand elasticity). And, in *each one of these cases*, he substituted an elasticity that would produce even greater impacts on production and prices than would even the elasticities used for purposes of the original modeling exercise.[114]

Supply and Demand Elasticities Used in Sumner I and II

Parameter	Effects of change to Sumner II elasticity (impact on world price due to removal of marketing loans and counter-cyclical payments)	Sumner I(FAPRI)	Sumner II(CATO)
U.S. cotton supply elasticity	INCREASED IMPACT	0.361 - 0.466	0.80
ROW cotton supply elasticity	INCREASED IMPACT	0.30	0.20
US mill demand elasticity	no change	-0.20	-0.20
US stocks demand elasticity	INCREASED IMPACT	-1.40*	no
ROW mill demand elasticity	INCREASED IMPACT	-0.25	-0.20
ROW stocks demand elasticity	INCREASED IMPACT	-0.463*	no

* Parameter estimate not presented in original Sumner model; estimates drawn from FAPRI model documentation discussed in Annex I to the US Rebutal Submission, paras 23-25. (Exhibit US-56, Exhibit US-109, Exhibit US-65)

81. In Brazil's "oral" presentation, it offers no justification for the flaws in the Sumner II model's structure or its arbitrary and unfounded elasticity assumptions. Nonetheless, the United States addresses below a few of the key aspects of Brazil's "oral" presentation regarding its modeling exercise.

82. First, the United States notes that Brazil continues to attempt to discredit the FAPRI model that it relied upon in the original proceeding (and that Brazil goes as far as to assert *the original panel* relied upon).[115] Now, for example, Brazil derides the years of research embodied in the FAPRI framework and parameters by characterizing it as "piece-mill development." This is presumably intended to establish the superiority of Brazil's model, which was developed by Dr. Sumner alone

[112] Daniel A. Sumner. "Boxed In: Conflicts Between U.S. Farm Policies and WTO Obligations." Center for Trade Policy Studies, The Cato Institute, December 2005. (Exhibit US-108)

[113] Daniel A. Sumner. "Boxed In: Conflicts Between U.S. Farm Policies and WTO Obligations." Center for Trade Policy Studies, The Cato Institute, December 2005. (Exhibit US-108)

[114] Of course, many of the elasticities in the model used for purposes of the original proceeding were already overstated.

[115] *See e.g.*, Brazil Rebuttal Submission, para. 292. Brazil neglects to mention, however, that the original panel expressly stated that "[w]e have taken note of the outcomes of the simulations submitted by Brazil1, and the parties' exchanges of views thereon. We have not relied upon the quantitative results of the modelling exercise – in terms of estimating any numerical value for the effects of the United States subsidies, nor, indirectly, in our examination of the causal link required under Articles 5 and 6.3(c) of the *SCM Agreement*."

after the original panel proceeding and which has never been subjected to any peer review or examination. Brazil's criticisms are remarkable given that – in an effort to have the original panel accept its allegedly FAPRI-based model in the original proceeding – Brazil specifically lauded the fact that FAPRI "continually update[d] [its] analytical capabilities and . . . market intelligence."[116] Thus, the fact that Brazil's new Sumner II model has not been subjected to the same kind of peer review and development renders it less – not more – reliable than the FAPRI framework.

83. Second, Brazil now claims that FAPRI parameters are inappropriate for analyzing the "permanent" removal of payments such as the marketing loan and counter-cyclical payments.[117] However, in the original proceeding Brazil asserted that "FAPRI is the most influential organization in the United States analyzing farm policy and its effects on U.S. and world commodity markets, i.e., that has the highest reputation and experience *in answering the kind of "but for" questions faced by this Panel*,"[118] Indeed, as Brazil expressly acknowledged in the original proceeding:

> The FAPRI model has been widely used for policy analysis in the United States and elsewhere for almost 20 years. U.S. commodity groups, including the U.S. cotton industry, have regularly used the FAPRI model to analyze farm commodity program options. The FAPRI model is also the key model used by the U.S. Congress in considering farm program options. For almost two decades the U.S. Congress has provided special appropriations to support the continued use and development of the FAPRI model. In both the 1996 and the 2002 Farm Bill processes, the FAPRI model provided the most influential projections of likely program impacts. FAPRI received the USDA highest honour for its analysis of certain proposals leading to the adoption of the 2002 FSRI Act.[119]

84. FAPRI has used their modeling system to analyze the removal of domestic subsidies under trade liberalization scenarios and the reduction of farm subsidies under various farm bill scenarios, including the "permanent" removal of payments. Indeed, in attempting to argue that elimination of the Step 2 program has had no effects on exports or prices, Brazil itself submitted and repeatedly cites to a FAPRI assessment of the effects of eliminating that program.[120] FAPRI economists did not find it necessary to change their model or modeling parameters to address that question (involving a total and permanent removal of payments). And Brazil did not complain that the FAPRI assessment of eliminating the Step 2 program was "biased downwards." To the contrary, in that context, Brazil *wants* the Panel to accept that FAPRI allegedly shows "relatively modest effects from the removal of the Step 2 subsidy." Brazil argues that the Panel should *rely* on FAPRI's analysis of that scenario in assessing the effects of eliminating the Step 2 program. Yet Brazil asserts that the same FAPRI analysis is somehow inappropriate for analyzing the counterfactual situation without marketing loan and counter-cyclical payments.[121] Brazil's arguments in this regard are internally inconsistent and lack credibility.

85. Third, the United States notes that Brazil has applied a long-run elasticity for U.S. supply response while imposing very conservative short-run elasticities for international supply and demand response. If the analysis is to be performed in the long run – and the United States considers that it must for the reasons explained at the meeting with the Panel – then long-run elasticities must be

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[116] Answers of Brazil to Questions from the Panel After 2nd Meeting, para 21 (22 December 2003).

[117] Brazil Oral Statement, para. 103.

[118] Answers of Brazil to Questions from the Panel After 2nd Meeting, para 24 (22 December 2003) (emphasis added).

[119] Brazil Further Submission, para. 214 (9 September 2003).

[120] *See* Brazil First Written Submission, para. 203 (addressing FAPRI, "Impacts of Commodity and Conservation Reserve Program Provisions in House and Senate Reconciliation Bills," FAPRI-UMC Report #15-05, December 2005(Exhibit Bra-484).)

[121] Brazil Oral Statement, para. 103.

assumed throughout the model. In that time, foreign cotton producers will make full adjustments and respond as well. Similarly, over the long-term, U.S. and foreign mill demand become more responsive to permanent price changes. There is no basis whatsoever for the kind of mix-and-match approach that Brazil has adopted in an effort to exaggerate any possible effects of the marketing loan and counter-cyclical payments.

86. Fourth, another key source of bias in Dr. Sumner's analysis is the fact that it does not incorporate, either explicitly or implicitly, any stock behaviour.[122] Yet, stock adjustments may have important effects on overall price movements in the short-run. As future prices increase relative to current prices, warehouses will tend to carry more inventory, choosing to sell their cotton in future periods when prices are higher. Likewise, if current prices are high relative to futures prices, sellers find it more attractive to market their cotton rather than holding it for sale in the future. In this way, stocks act to buffer prices. If prices fall, potential sellers will sell less and hold more in stock, thus bolstering prices. If prices rise, inventory holders will sell stocks, thus dampening prices. Ignoring stockholding behaviour in the kind of predominantly short-run assessment that Brazil attempts to conduct exacerbates any possible effects of removal of marketing loans and counter-cyclical payments on world price.

87. Fifth, the United States contests Brazil's efforts to explain away the fact that it uses counter-cyclical payments rates that are in excess of the statutory maximum. According to Dr. Sumner, this results from calculation of counter-cyclical payment rates on a per-pound of production basis[123]: "[The Sumner II model] uses the CCP rate per pound of production for each year. Since cotton production is smaller than cotton base, the CCP rate per pound of production can exceed 13.73 cents per pound when the CCP rate per pound of base remains at the maximum."[124] In other words, Brazil admits that it attempts to attribute to upland cotton production *all* counter-cyclical payments made in respect of upland cotton base acres regardless of whether upland cotton or some other crop was grown. More precisely, Brazil attempts to attribute *cotton* production-inducing effects in respect of payments even when the payments were made on farms that did not produce upland cotton or on farms where other crops were grown, instead of upland cotton, on acres historically planted to cotton. This is an illogical approach that serves no purpose other than to inflate the results of the modeling exercise.

88. In sum, the evidence and arguments before the Panel show that the Sumner II model lacks the rigor or detail to address the complexities of the global fiber market. Moreover, the model's choice of elasticities introduces biased results. Even ignoring the structural issues with the model, the United States has demonstrated that the use of more reasonable, independent elasticities produce dramatically smaller impacts on world price.

IV. CONCLUSION

89. The United States has implemented the DSB's recommendations and rulings in this dispute and that it has done so consistently with its WTO obligations. The United States has eliminated two export credit guarantee programs entirely. And the United States has substantially overhauled the third, lowest-risk program. The United States has also eliminated a third program, the Step 2 program, payments under which were claimed by Brazil to be prohibited export subsidies, among the most distortive of subsidy measures.

90. Moreover, substantial evidence confirms that payments under the marketing loan and counter-cyclical payment programs are not causing present significant price suppression, as Brazil alleges.

[122] The absence of such an analysis is especially remarkable given Brazil's new theory that it is stocks – not exports – that are suppressing world market prices.

[123] Brazil Oral Statement, para. 120.

[124] Brazil Oral Statement, para. 120.

Brazil has not been able to rebut this evidence. Rather, it continues to rely on the heavily biased results of the modeling exercise commissioned for purposes of this dispute. The United States has shown that exercise to be unreliable and, as its author has noted in another context, not "appropriate to support [Brazil's] serious prejudice claim before [this] WTO panel."[125]

91. Finally, the United States again would like to thank the Panel for providing this opportunity to comment on Brazil's "oral" statement. While we recognize that such an opportunity is unusual in WTO panel proceedings, the approach taken by Brazil to the Panel meeting was, itself, unusual. Brazil's approach had the unfortunate consequence of limiting the chance for an oral dialogue with the Panel to a single afternoon. Fortunately, by allowing this opportunity for comment, the Panel has allowed the dialogue to take place, albeit in written form.

[125] Daniel A. Sumner. "Boxed In: Conflicts Between U.S. Farm Policies and WTO Obligations." Center for Trade Policy Studies, The Cato Institute, December 2005. (Exhibit US-108)

ANNEX

CALCULATION OF EXPECTED MARKET NET RETURNS ABOVE VARIABLE COSTS

1. Expected Market Prices:

For upland cotton, soybeans and corn, the expected market price is based on the January-March average of the relevant harvest-time (futures) contract. This is the expected market price most likely to be relied upon by a producer. For 2007, since data are not available for the full month of March, the average reflects January 1 through March 2. The source for those prices is the New York Board of Trade for cotton futures; Chicago Board of Trade for corn and soybeans.

Using the relevant harvest-time contract, the expected market price is derived by subtracting an average basis from the futures price. In the case of cotton, the basis used is $0.05 per pound. For soybeans and corn, a basis of $0.14 is used for each. The basis was taken from analysis by USDA/ERS that projects market prices and counter-cyclical payment rates from futures prices. Models can be found at http://www.ers.usda.gov/Data/PriceForecast/.

For cottonseed, in the absence of a futures market to determine price expectations, expected market prices are set at lagged prices.

2. Expected Yields

For all crops, expected yields are determined based on a linear trend equation applied to USDA/NASS data for actual yields for the period 1995-2006. For upland cotton and cottonseed, the expected yield represents an average yield across the 17 cotton-producing states. For soybeans and corn, average yields across the Cotton Belt are also used, with the exception of data for Missouri and Kansas. Both states are relatively small producers of cotton and large producers of corn and soybeans. However, the majority of corn and soybeans are grown in parts of the states too far north to be suitable for cotton production. Corn and soybean yields in those regions, therefore, are not directly applicable to corn and soybean yields that would be expected in the cotton producing regions of those states.

3. Variable Costs

Data for variable costs are taken from USDA/ERS costs of production data. For each crop, operating costs and hired labor are included as variable costs. For cotton, the costs represent the average across the Cotton Belt. In the case of competing crops, regional data are used to calculate average costs across the cotton-producing states to most closely match the costs faced by U.S. farmers.[1] Projected cotton-belt costs for corn and soybeans are derived from USDA/ERS projections of national costs.

4. Expected Market Net Returns

For 2002 through 2007, expected market returns above variable costs are calculated as follows:

(a) For cotton, variable costs (including USDA-designated costs assigned to ginning that exceed revenue from cottonseed and hired labor) are subtracted from market returns for cotton lint.

(b) For soybeans and corn, variable costs are subtracted from market returns for each of the crops.

[1] The United States does not use national average costs for corn and soybeans since those costs are heavily influenced by the Midwestern United States. Although the majority of corn and soybean production occurs there, it is an area that is not suitable for cotton production. Therefore, the costs for those regions are not the costs ordinarily faced by U.S. cotton farmers.

ANNEX D-6

RESPONSES OF BRAZIL TO THE PANEL'S FIRST SET OF QUESTIONS (SECTIONS A-C)

(26 February 2007)

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Australia – Leather (21.5)	Panel Report, *Australia – Subsidies Provided to Producers and Exporters of Automotive Leather*, WT/DS126/RW, adopted 11 February 2000, DSR 2000:III, 1189.
Australia – Salmon (Article 21.5 – Canada)	Panel Report, *Australia – Measures Affecting Importation of Salmon – Recourse to Article 21.5 of the DSU by Canada*, WT/DS18/RW, adopted 20 March 2000, DSR 2000:IV, 2031.
Canada – Aircraft (21.5)	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft – Recourse by Brazil to Article 21.5 of the DSU*, WT/DS70/AB/RW, adopted 4 August 2000, DSR 2000:IX, 4299.
Canada – Dairy (21.5)	Appellate Body Report, *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products – Recourse to Article 21.5 of the DSU by New Zealand and the United States*, WT/DS103/AB/RW, WT/DS113/AB/RW, adopted 18 December 2001, DSR 2001:XIII, 6829.
Chile – PBS (21.5)	Panel Report, *Chile – Price Band System and Safeguard Measures Relating to Certain Agricultural Products – Recourse to Article 21.5 of the DSU by Argentina*, WT/DS207/RW, circulated to WTO Members 8 December 2006.
EC – Bed Linen (21.5)	Appellate Body Report, *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India – Recourse to Article 21.5 of the DSU by India*, WT/DS141/AB/RW, adopted 24 April 2003, DSR 2003:III, 965.
EC – Bed Linen (21.5)	Panel Report, *European Communities – Anti-Dumping Duties on Imports of Cotton-Type Bed Linen from India – Recourse to Article 21.5 of the DSU by India*, WT/DS141/RW, adopted 24 April 2003, modified by Appellate Body Report, WT/DS141/AB/RW, DSR 2003:IV, 1269.
EC – Selected Customs Matters	Appellate Body Report, *European Communities – Selected Customs Matters*, WT/DS315/AB/R, adopted 11 December 2006.
Mexico – Corn Syrup (21.5)	Appellate Body Report, *Mexico – Anti-Dumping Investigation of High Fructose Corn Syrup (HFCS) from the United States – Recourse to Article 21.5 of the DSU by the United States*, WT/DS132/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6675.
U.S. – Certain EC Products (21.5)	Panel Report, *United States – Import Measures on Certain Products from the European Communities*, WT/DS165/R and Add.1, adopted 10 January 2001, modified by Appellate Body Report, WT/DS165/AB/R, DSR 2001:II, 413.
U.S. – FSC	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations"*, WT/DS108/AB/R, adopted 20 March 2000, DSR 2000:III, 1619.
U.S. – FSC (21.5 II)	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Second Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW2, adopted 14 March 2006.
U.S. – FSC (21.5 II)	Panel Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Second Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/RW2, adopted 14 March 2006, upheld by Appellate Body Report, WT/DS108/AB/RW2.
U.S. – Shrimp (21.5)	Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products – Recourse to Article 21.5 of the DSU by Malaysia*, WT/DS58/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6481.
U.S. – Softwood Lumber IV (21.5)	Appellate Body Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada – Recourse by Canada to Article 21.5 of the DSU*, WT/DS257/AB/RW, adopted 20 December 2005.

Short Title	Full Case Title and Citation
U.S. – Softwood Lumber IV (Article 21.5)	Panel Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada – Recourse by Canada to Article 21.5 [of the DSU]*, WT/DS257/RW, adopted 20 December 2005, upheld by Appellate Body Report, WT/DS257/AB/RW.
US – Softwood Lumber V	Appellate Body Report, *United States – Final Dumping Determination on Softwood Lumber from Canada*, WT/DS264/AB/R, adopted 31 August 2004, DSR 2004:V, 1875.
US – Softwood Lumber VI (21.5)	Appellate Body Report, *United States – Investigation of the International Trade Commission in Softwood Lumber from Canada – Recourse to Article 21.5 of the DSU by Canada*, WT/DS277/AB/RW, adopted 9 May 2006.
U.S. – OCTG Sunset Reviews (21.5)	Panel Report, *United States – Sunset Reviews of Anti-Dumping Measures on Oil Country Tubular Goods from Argentina – Recourse to Article 21.5 of the DSU by Argentina*, WT/DS268/RW, circulated to WTO Members 30 November 2006.
US – OCTG Sunset Reviews (Argentina)	Appellate Body Report, *United States – Sunset Reviews of Anti-Dumping Measures on Oil Country Tubular Goods from Argentina*, WT/DS268/AB/R, adopted 17 December 2004, DSR 2004:VII, 3257.
U.S. – Upland Cotton	Appellate Body Report, *United States – Subsidies on Upland Cotton*, WT/DS267/AB/R, adopted 21 March 2005.
U.S. – Upland Cotton	Panel Report, *United States – Subsidies on Upland Cotton*, WT/DS267/R, and Corr.1, adopted 21 March 2005, modified by Appellate Body Report, WT/DS267/AB/R.

A. GENERAL QUESTIONS

Questions to both parties

1. Is Brazil/US of the view that a party to a dispute referred to a panel established under Article 21.5 of the DSU (a party in a compliance panel) can make the same legal argument as it did in the original Panel proceedings?

1. Brazil notes that a party's *arguments* in WTO dispute settlement are distinct from the *claims* identified by the complaining Member in the request for the establishment of a panel.[1] Although there are certain limitations on the *claims* that can be brought by the complainant in Article 21.5 proceedings, the complaining and respondent Members are free to make whatever legal *arguments* they wish.

2. Could each party explain its view on the question of whether, and to what extent, this Panel must rely on the legal and factual analysis underlying the original panel's findings? What are the relevant provisions of the DSU in this regard?

2. According to Article 3.2 of the DSU, dispute settlement is a central element in providing "*security and predictability* to the multilateral trading system". In developing a dispute settlement system that contributes to securing this objective, panels and the Appellate Body have taken care to ensure that disputes involving the same or similar factual and legal questions are resolved in the same way. The Appellate Body has articulated principles in this regard that seek to further the goals of security and predictability.[2]

3. *First*, prior adopted panel and Appellate Body reports create "legitimate expectations" among WTO Members, and should be taken into account by panels when they are relevant to the resolution of a dispute.[3] *Second*, where the issues before a panel are the same as those previously examined by the Appellate Body, it is "not only appropriate," but to "be expected," that the panel would follow the Appellate Body's earlier conclusions.[4]

4. The Appellate Body has also clarified that the objective of "security and predictability" applies with particular force in Article 21.5 proceedings. As Brazil noted in previous submissions, the Appellate Body has stated that "Article 21.5 proceedings do not occur in isolation but are part of a '*continuum of events*.'"[5] The Appellate Body observed that "doubts could arise about the *objective nature* of an Article 21.5 panel's assessment if, on a specific issue, that panel were to *deviate* from the reasoning in the original panel report in the absence of any change in the underlying evidence."[6]

5. In this passage, the Appellate Body linked the need for consistent decision-making by a compliance panel to that panel's duty to make an "objective assessment" of the matter under Article 11 of the DSU. If a compliance panel "deviate[d]" from the original panel's findings on a "specific issue", without a fundamental change in the domestic legal framework and/or facts warranting this deviation, it would suggest that the compliance panel is acting in an arbitrary fashion that does not meet the requirements of an "objective assessment". Accordingly, in the progression of

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[1] *See, e.g.*, Appellate Body Report, *EC – Selected Customs Matters*, para. 153.

[2] *See* Appellate Body Report, *US – Softwood Lumber V*, para. 111, where the Appellate Body expressly relied on Article 3.2 of the DSU.

[3] Appellate Body Report, *US – Softwood Lumber V*, para. 111.

[4] Appellate Body Report, *US – OCTG Sunset Reviews (Argentina)*, para. 188.

[5] Appellate Body Report, *U.S. – Softwood Lumber IV (21.5)*, para. 103 (emphasis added) citing Appellate Body Report, *Mexico – Corn Syrup (21.5)*, para. 121. *See* Brazil's First Written Submission, para. 28.

[6] Appellate Body Report, *US – Softwood Lumber VI (21.5)*, para. 103 (emphasis added).

"events" within a single dispute, it is especially important for the compliance panel to respect the findings of the panel and the Appellate Body in the original proceedings.

6. In this compliance dispute, with respect to Brazil's claims of adverse effects, many of the legal questions have already been addressed by the original panel and the Appellate Body. The structure, design and operation of the contested subsidy programs has not altered, nor has the general order of the magnitude of these subsidies. Indeed, the magnitude of the subsidies has *increased*. Further, the evidence relating to the effect of the contested subsidies in the marketplace is also very much the same. In these circumstances, the requirements of "security and predictability," and an "objective assessment", require the compliance Panel to follow the relevant findings of the original panel and the Appellate Body.

7. Although a compliance panel should follow the findings of the original panel and Appellate Body when the factual and legal questions are the same, the questions that arise in compliance proceedings may differ. This is because a compliance panel "is not confined to examining the 'measures taken to comply' from the perspective of the claims, arguments and factual circumstances that related to the measure that was the subject of the original proceedings."[7]

8. With respect to the claims regarding export credit guarantees, the factual and legal questions relating to the existence of a "benefit" under Article 1.1(b) of the *SCM Agreement* were not addressed by the panel in the original proceedings. Thus, there are no findings on these questions that the compliance panel should follow. Brazil notes, however, that prior panel reports address how to assess the "benefit" from loan guarantees[8]; those reports create "legitimate expectations" among WTO Members on this specific issue, and should be taken into account by the compliance panel.[9] The factual and legal questions relating to item (j) of the Illustrative List of Export Subsidies have been thoroughly explored in the original proceedings. To ensure "security and predictability", the compliance panel should follow the earlier findings in its interpretation of item (j) and in its treatment of the evidence.

B. QUESTIONS WITH RESPECT TO BRAZIL'S REQUEST UNDER ARTICLE 13.1 DSU

Questions to the US

3. Is the United States arguing that Brazil must identify the subsidized product for each of the types of subsidies from which it claims serious prejudice? Is the United States arguing that payments which permit planting flexibility are not tied to the production of upland cotton, so that they must be allocated by Brazil across the total value of production of each recipient?

4. Does the United States contest the accuracy of the figures for 2003 – 2005 cited in "Table 6"[10] of Brazil's first submission and "Table 5"[11] of Brazil's rebuttal submission? If so, please provide the accurate figures, or the figures the US deems to be more accurate.

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[7] Appellate Body Report, *Canada – Aircraft (21.5)*, para. 41. *See also* Panel Report, *Chile – PBS (21.5)*, paras. 7.129, 7.136-7.137. The Appellate Body later confirmed that this statement applied in the context of "a *new* claim challenging a *new* component of the measure taken to comply which was not part of the original measure." Appellate Body Report, *EC – Bed Linen (21.5)*, para. 88.

[8] *See* Panel Report, *EC – CVDs on DRAMs*, paras. 7.189, 7.190; Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.345.

[9] Appellate Body Report, *US – Softwood Lumber V*, para. 111.

[10] Immediately preceding para. 112 of Brazil's First Written Submission.

[11] Immediately following para. 173 of Brazil's Rebuttal Submission.

Question to Brazil

5. The Panel refers to Brazil's communication dated 22 January 2007 concerning its request in relation to Article 13.1 of the DSU. Is it correct for the Panel to understand that as far as data for 2005 is concerned, data included in Exhibit US-64 satisfies all of the requests Brazil made in Part A of Annex 1 of its 1 November communication?

9. The Panel is correct in understanding that the data included in Exhibit US-64, as far as marketing year 2005 is concerned, satisfies Part A of Brazil's 1 November 2006 request. The data enables Brazil to calculate the amount of counter-cyclical payments allocated to upland cotton under the "Cotton-to-Cotton Methodology" and under "Brazil's Methodology." Brazil presents the results of its calculation as part of its Opening Statement to the compliance Panel.

C. QUESTIONS CONCERNING THE PRELIMINARY OBJECTIONS RAISED BY THE UNITED STATES

1. Preliminary objections of the United States in respect of claims of Brazil regarding export credit guarantees in respect of pig meat and poultry meat

Question to both parties

6. The parties disagree with respect to whether in a proceeding under Article 21.5 of the DSU a party may present a claim that was raised in the original proceeding but on which no finding of WTO-inconsistency was made due to the fact that the Appellate Body was unable to complete the analysis.

a) Could the parties explain the legal basis in the text of Article 21.5 of the DSU and other relevant provisions of the DSU for their position on this question?

b) Could the parties explain whether and how their position on this issue is consistent with prior panel and Appellate Body reports?

A. Introduction

10. Brazil claims that the amended GSM 102 program has been applied to circumvent U.S. export subsidy commitments on pig meat and poultry meat, in contravention of Articles 10.1 and 8 of the *Agreement on Agriculture* (and in consequence, of Articles 3.1(a) and 3.2 of the *SCM Agreement*). In its response to this question, Brazil will demonstrate that under the relevant provisions of the DSU and the jurisprudence, its claims are properly within the scope of these Article 21.5 proceedings. Brazil will address the limits placed by the DSU and prior jurisprudence on both the measures that may be challenged in Article 21.5 proceedings, and the claims that can be raised against those measures. Brazil will then demonstrate that its claims, and the measure subject to those claims, observe those limits.

B. Background

11. The treatment of Brazil's claims in the original proceedings is important to the compliance Panel's assessment of the United States' preliminary objection. In the original proceedings, the measure at issue was the original GSM 102 program, which had general terms and conditions that applied on a non-product-specific basis to many agricultural products. Brazil claimed that this measure involved export subsidies applied in a manner that circumvented the United States' export subsidy commitments for all thirteen of its scheduled products and for unscheduled products, under Article 10.1 of the *Agreement on Agriculture*.

12. The original panel found that Brazil had demonstrated application by the United States of GSM 102 to circumvent U.S. export subsidy commitments for "unscheduled" products and for one "scheduled" product – rice. On appeal, Brazil challenged the original panel's failure to find that the export credit guarantees ("ECG") programs were applied in a manner which results in circumvention of U.S. export subsidy commitments for three other scheduled products – pig meat, poultry meat and vegetable oil.[12] At the oral hearing, Brazil withdrew its appeal with respect to vegetable oil.[13]

13. On review, the Appellate Body reversed the original panel's finding that Brazil had failed to demonstrate actual circumvention with respect to pig meat and poultry meat.

14. However, the Appellate Body concluded that there were insufficient uncontested facts of record to enable it to complete the analysis.[14] Because the Appellate Body was unable to complete the analysis, there is no adopted finding that the original GSM 102 program is applied in a manner that circumvents the United States' commitments with respect to pig meat and poultry meat. At the same time, however, there is also no adopted finding that the original GSM 102 program, again with respect to pig meat and poultry meat, is not inconsistent with Article 10.1 of the *Agreement on Agriculture*.

15. During implementation, the United States could have taken steps to amend the GSM 102 program exclusively with respect to the terms and conditions applicable to rice and unscheduled products. However, it did not do so. Instead, it revised the general terms and conditions of the program, including the guarantee fee schedule, adopting an amended GSM 102 program that still applies on a non-product-specific basis. In adopting an amended GSM 102 program, the United States was obliged to ensure that this new measure respected all of the United States' obligations under the covered agreements.

16. In these compliance proceedings, Brazil claims that the amended GSM 102 program is not consistent with the United States' obligations under, among others, Article 10.1 of the *Agreement on Agriculture* because this new measure is applied in a manner that circumvents U.S. obligations with respect to three scheduled products – pig meat, poultry meat and rice – and unscheduled products.

17. There is no dispute between the Parties that this claim is included in Brazil's request for establishment, which states, in relevant part, as follows:

> ... [S]ubsequent to 1 July 2005, ECGs [export credit guarantees] under the GSM 102 and SCGP [Supplier Credit Guarantee] programs have been applied to circumvent US export subsidy commitments, within the meaning of Article 10.1 of the *Agreement on Agriculture*. Brazil is concerned that ECGs under the GSM 102 and SCGP programs have been provided subsequent to 1 July 2005 to support the export of: upland cotton and other unscheduled products; and, rice, **pigmeat and poultry meat**, in excess of US reduction commitment levels for those products.[15]

18. Brazil now turns to consider whether there are any limitations in these compliance proceedings on its right (1) to challenge the amended GSM 102 program in these proceedings as a "measure taken to comply" or (2) to claim that this new measure circumvents the United States' export subsidy commitments for pig meat and poultry meat.

19. The DSU contains limits on: (i) the measures that may properly be subject to review in Article 21.5 proceedings; and, (ii) the claims that may properly be subject to review in Article 21.5 proceedings. Brazil will address these two limits – on measures, and on claims – separately.

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[12] Appellate Body Report, *U.S. – Upland Cotton*, para. 683.
[13] Appellate Body Report, *U.S. – Upland Cotton*, para. 683.
[14] Appellate Body Report, *U.S. – Upland Cotton*, paras. 689-694.
[15] WT/DS267/30, para. 27 (emphasis added).

20. The distinction between measures and claims is important, given the basis for the United States' objection.

C. Measures

1. Limits on **measures** subject to Article 21.5 review

21. Article 21.5 enables a compliance panel to review claims regarding the existence, or the consistency with the covered agreements, of "measures taken to comply" with the recommendations and rulings of the DSB. Measures that are not "taken to comply" with the DSB's recommendations and rulings may not be pursued in Article 21.5 proceedings.[16]

22. According to the Appellate Body, the phrase "measure taken to comply" in Article 21.5 includes a new measure "in its totality".[17] Exactly what constitutes the bounds of a "measure taken to comply" varies according to the circumstances of the dispute, however.

2. Erroneous basis for U.S. objection and the relevance of that objection for assessment of "measures"

23. In these proceedings, Brazil has fully observed the limits on the measures subject to Article 21.5 review.

24. In its Rebuttal Submission, the United States clarifies that Brazil's claim is not properly within the scope of these Article 21.5 proceedings because it relates to a measure that is not a "measure taken to comply". The United States describes the "measure" subject to Brazil's claim as "pig meat and poultry meat GSM 102 guarantees".[18] The United States argues that such a "measure" could not be a "measure taken to comply", because there was no recommendation compelling action with respect to "pig meat and poultry meat GSM 102 guarantees".[19]

25. With these statements, the United States confounds Brazil's claim, and the measure that is the subject of that claim.

26. As noted above, Brazil's claims of inconsistency are product-specific with respect to scheduled products, as they must be.[20] Article 10.1 prohibits the use of export subsidies not listed in

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[16] Appellate Body Report, *Canada – Aircraft (21.5)*, para. 36 ("Proceedings under Article 21.5 do not concern just *any* measure of a Member of the WTO; rather, Article 21.5 proceedings are limited to those 'measures *taken to comply* with the recommendations and rulings' of the DSB. In our view, the phrase 'measures taken to comply' refers to measures which have been, or which should be, adopted by a Member to bring about compliance with the recommendations and rulings of the DSB. In principle, a measure which has been 'taken to comply with the recommendations and rulings' of the DSB will *not* be the same measure as the measure which was the subject of the original dispute, so that, in principle, there would be two separate and distinct measures: the original measure which *gave rise* to the recommendations and rulings of the DSB, and the 'measures taken to comply' which are – or should be – adopted to *implement* those recommendations and rulings.").

[17] Appellate Body Report, *U.S. – Softwood Lumber IV (21.5)*, para. 67; Appellate Body Report, *U.S. – Shrimp (21.5)*, para. 87.

[18] U.S. Rebuttal Submission, para. 10 ("In other words, as Brazil expressly concedes, there have *never* been any findings of WTO inconsistency against the pig meat and poultry meat GSM 102 guarantees, and consequently there were no DSB recommendations and rulings against these measures with which the United States was obligated to comply.") (emphasis added). *See also Id.*, paras. 14, 15.

[19] U.S. Rebuttal Submission, para. 10.

[20] *See also* Brazil's Rebuttal Submission, para. 378. Consistent with its request for establishment, Brazil's claims concerning GSM 102 ECGs for *unscheduled* products are also product-specific, since they are limited to *any* unscheduled product that has received GSM 102 support subsequent to 1 July 2005.

Article 9.1 of the *Agreement* to circumvent (or threaten to circumvent) "export subsidy commitments". The first clause of Article 3.3 of the *Agreement on Agriculture* specifies that with respect to scheduled products, those "export subsidy commitments" include the commitment not to provide export subsidies "in excess of the budgetary outlay and quantity commitments levels specified" in its Schedule.[21]

27. To establish its product-specific claims of circumvention with respect to scheduled products, Brazil has established: (i) that in FY 2006, the United States provided GSM 102 ECGs to support the export of rice, pig meat and poultry meat in excess of its annual quantity commitment levels for those products; and, (ii) that during the period 1 July – 30 September 2005, the United States provided GSM 102 ECGs to support the export of rice and poultry meat in excess of its annual quantity commitment levels for those products.[22]

28. In contrast, the measure subject to Brazil's claims of inconsistency with the covered agreements is not product-specific, as the United States asserts. The measure subject to Brazil's claims of inconsistency, "in its totality"[23], is the GSM 102 program as amended by the United States' "measures taken to comply" – the modification of the GSM 102 fee schedule (including the removal of certain risk categories from eligibility).[24]

29. There is no factual basis for the United States to characterize the measure subject to Brazil's claims of inconsistency as "the pig meat and poultry meat GSM 102 guarantees".[25] No such "measure" exists. Neither the amended GSM 102 program in its totality, nor the individual amendments, set out terms or conditions that differ as between different eligible products:

- Fees under the amended GSM 102 schedule effective 1 July 2005 differ according to country risk, repayment term and repayment frequency, but not according to the eligible products involved.[26]

- The regulations relating to the GSM 102 program do not set out differing terms and conditions for GSM 102 ECGs depending on the specific eligible product at issue.[27]

- The USDA FAS press release announcing amendments to the ECG programs effective 1 July 2005 does not indicate that those amendments apply differently to different eligible products[28];

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[21] *See* Appellate Body Report, *U.S. – FSC*, para. 145. In an export subsidy dispute involving products listed in Annex I to the *Agreement on Agriculture*, Article 3 of the *SCM Agreement* also applies on a product-specific basis. The *chapeau* to Article 3.1 prohibits export subsidies "[e]xcept as provided in the Agreement on Agriculture". If export subsidies are provided for products listed in Annex I to the *Agreement on Agriculture* within the limits of a Member's "export subsidy commitments" – meaning, for scheduled products, below the Member's budgetary outlay and quantity commitments levels specified in its Schedule – the safe harbour in the *chapeau* to Article 3.1 applies.

[22] Exhibits Bra-552, Bra-553 and Bra-554. *See also* Brazil's First Written Submission, para. 452.

[23] Appellate Body Report, *U.S. – Softwood Lumber IV (21.5)*, para. 67; Appellate Body Report, *U.S. – Shrimp (21.5)*, para. 87.

[24] *See* WT/DS267/30, paras. 8 ((ii) and (iii)), 26. Throughout its response, Brazil will refer to the measure subject to its claims as "the GSM 102 program as amended by the modified GSM 102 fee schedule".

[25] U.S. Rebuttal Submission, para. 10.

[26] Exhibit Bra-504 ("USDA changes its fees to risk-based method for the GSM-102 and Supplier Credit Guarantee programs," USDA FAS Online News Release, 30 June 2005, accessed November 2006 at http://www.fas.usda.gov/scriptsw/PressRelease/pressrel_dout.asp?PrNum=0093-05); Exhibit Bra-505 (GSM-102 Guarantee Fee Rate Schedule, USDA FAS Online, accessed September 2006 at www.fas.usda.gov/excredits/gsm102fees.html).

[27] Exhibit Bra-519 (7 C.F.R. Part 1493, Subparts A and B, GPO Access Online, January 2006, accessed July 2006 at http://www.gpoaccess.gov/cfr/index.html).

- USDA FAS "FAQs" issued with the announcement of the amendments to the ECG programs effective 1 July 2005 does not indicate that those amendments apply differently to different eligible products[29];

- The USDA FAS "fact sheet" describing the amendments to the ECG programs effective 1 July 2005 does not indicate that those amendments apply differently to different eligible products.[30]

30. The measure subject to Brazil's claims in this dispute, and the GSM 102-related "measures taken to comply", are identical – namely, the GSM 102 program as amended by the modified GSM 102 fee schedule. The measure does not apply on a product-specific basis; the terms and conditions for ECGs under the GSM 102 program as amended by the modified GSM 102 fee schedule are the same for pig meat, poultry meat, and all other eligible scheduled as well as unscheduled products. While Brazil's claims regarding the consistency of the GSM 102 program as amended by the modified GSM 102 fee schedule are product-specific, the measure at issue is not.

31. The United States' objection to the inclusion of Brazil's Article 10.1 claims concerning pig meat and poultry meat within the scope of these Article 21.5 proceedings, is that those claims identify a *product-specific* measure. That objection is misplaced and should be rejected.[31] By challenging the amended GSM 102 program, Brazil is in full compliance with the limits imposed by Article 21.5 on the measures that may properly be subject to Article 21.5 review.

D. Claims

1. Erroneous basis for U.S. objection and the relevance of that objection for assessment of "*claims*"

32. As noted, the contested measure taken to comply – the GSM 102 program as amended by the modified GSM 102 fee schedule – applies uniformly and without variation to all eligible products. In these Article 21.5 proceedings, Brazil's claims apply to GSM 102 support for only some of those eligible products – unscheduled products and three scheduled products – rice, pig meat and poultry meat.

33. Given the Appellate Body's inability to complete the analysis with respect to Brazil's product-specific claims concerning support for exports of pig meat and poultry meat[32], there is no final resolution to Brazil's claims regarding the *original* GSM 102 program. Specifically, there are no adopted findings that the ECG programs, with respect to pig meat and poultry meat, are inconsistent with Article 10.1 of the *Agreement on Agriculture*, and there are no adopted findings that the ECG programs, again with respect to pig meat and poultry meat, are not inconsistent with Article 10.1.

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[28] Exhibit Bra-502 ("USDA announces changes to export credit guarantee programs to comply with WTO Findings," USDA FAS Online News Release, 30 June 2005, accessed November 2006 at http://www.fas.usda.gov/scriptsw/PressRelease/pressrel_dout.asp?PrNum=0092-05).

[29] Exhibit Bra-501 ("FAQs: Risk-Based Fees," Foreign Agriculture Service, USDA, accessed November 2006 at www.fas.usda.gov/excredits/faqs.html).

[30] Exhibit Bra-520 ("Export Credit Guarantee Program," USDA FAS Fact Sheet, March 2006, accessed November 2006 at http://www.fas.usda.gov/info/factsheets/gsm102-03.asp).

[31] As a result, the manifestations of "potential procedural unfairness" identified by the compliance Panel in *U.S. – Certain EC Products (21.5)*, which arose from the fact that the EC was bringing a new claim against an aspect of the original measure that remained unchanged following adoption by the United States of its "measures taken to comply", do not arise in the current compliance proceedings. Panel Report, *U.S. – Certain EC Products (21.5)*, para. 7.75 (note 294).

[32] Appellate Body Report, *U.S. – Upland Cotton*, paras. 689-694.

34. The United States does not appear to challenge the "final resolution" standard *per se*. That is, the basis for the United States' objection is not that Brazil is prohibited from pursuing the same claims that it maintained in the original proceedings, where there has not been final resolution of those claims. Rather, as discussed above, the United States argues that Brazil is prohibited from pursuing those same claims in these Article 21.5 proceedings, because the claims concern a measure that is not a "measure taken to comply".

35. Brazil has demonstrated above that its claims concern a *new* "measure taken to comply" that replaces the original measure. That is, the original GSM 102 program has been replaced by the amended GSM 102 program, including a modified guarantee fee schedule. In the situation where the Article 21.5 proceedings concern a new aspect of a new measure, there are *no* limits on the scope of Brazil's claims in these proceedings. The text of Article 21.5 allows claims regarding both the existence of measures taken to comply, and the consistency of those measures with all of the United States' obligations under the covered agreements.

36. The situation in these Article 21.5 proceedings is very similar to the situation that arose in the Article 21.5 proceedings in *Canada – Aircraft*. In that dispute, Canada amended the terms and conditions of an export subsidy program.[33] The Appellate Body held that the "measure taken to comply" was "a new measure, the *revised* TPC program", which was "separate and distinct" from the *original* TPC program.[34] In this dispute, the United States also amended the terms and conditions of an export subsidy program. The "measure taken to comply" is, therefore, "a new measure, the *revised* [GSM 102] program".

37. With respect to a new measure, the Appellate Body held that a compliance panel operating under the authority of Article 21.5 "is not confined to examining the 'measures taken to comply' from the perspective of the claims, arguments and factual circumstances that related to the measure that was the subject of the original proceedings."[35] Thus, a compliance panel can assess any claims made with respect to the new measure. The Appellate Body expressly endorsed the view that the complaining Member can make the "*same*" claims that were made in the original proceedings.[36]

38. Thus, in these compliance proceedings, Brazil is entitled to claim that the amended GSM 102 program is applied in a manner that circumvents the United States' commitments for pig meat and poultry meat.

39. The compliance Panel's asks Brazil to justify its position – that it may pursue, in Article 21.5 proceedings, the same claim that it maintained in the original proceedings, where there has not been final resolution of that claim – under the DSU, as interpreted by panels and the Appellate Body. Brazil explores the limits on claims that can be made in compliance proceedings in the paragraphs that follow.

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[33] Appellate Body Report, *Canada – Aircraft (21.5)*, para. 34.

[34] Appellate Body Report, *Canada – Aircraft (21.5)*, para. 36 (italics in original, underlining added).

[35] Appellate Body Report, *Canada – Aircraft (21.5)*, para. 41.

[36] Appellate Body Report, *Canada – Aircraft (21.5)*, footnote 35 (emphasis in original) ("We note that the claim made by Brazil relating to the revised TPC program, in this Article 21.5 dispute, is the *same* as the claim made by Brazil in the original proceedings in relation to the TPC program as previously constituted. In both cases, Brazil complained that the measure at issue was inconsistent with Article 3.1(a) of the *SCM Agreement*. These proceedings do not, therefore, involve a claim under a provision of the *SCM Agreement*, or, even, a claim under a covered agreement, that was not examined in the original proceedings in *Canada - Aircraft*.") (emphasis in original).

2. Limits on **claims** subject to Article 21.5 review

a. Limits concerning "**new**" claims

40. Several disputes have explored limits on the ability in Article 21.5 proceedings to pursue new claims regarding *unchanged* components of the *original* measure that were not pursued in the original proceedings. Panels have determined that a complaining Member may not, in Article 21.5 proceedings, pursue a new claim on an aspect of the original measure that remains unchanged from the original proceedings, and that was not challenged in the original proceedings.[37]

41. This line of jurisprudence is not relevant to the issue currently before the compliance Panel. The United States' objection does not relate to a new claim made by Brazil in these Article 21.5 proceedings, but instead relates to the same Brazilian claim made first in the original proceedings, and again in these Article 21.5 proceedings. This line of case-law is also irrelevant in this proceeding because Brazil's claims relate to the *changed* guarantee fee schedule of the amended GSM 102 program, and not to an *unchanged* aspect of the original measure.

b. Limits concerning the "**same**" claims: "final resolution" standard

42. Another line of disputes addresses limits on a complaining Member's ability to pursue the same claim, in Article 21.5 proceedings, that it had previously pursued in the original proceedings. On several occasions, the Appellate Body and compliance panels have explored the limits on the ability in Article 21.5 proceedings to pursue the same claims previously pursued in the original proceedings regarding an unchanged aspect of the original measure.

43. In *EC – Bed Linen (21.5)*, the Appellate Body concluded that[38]

> an *unappealed* finding included in a panel report that is *adopted* by the DSB must be treated as a *final resolution* to a dispute between the parties in respect of the *particular* claim and the *specific* component of a measure that is the subject of that claim.[39]

44. As noted in Brazil's 16 January submission[40], the situation posed by the Appellate Body is different from the circumstances in the present dispute. To recap, the original panel limited its findings regarding circumvention to unscheduled products and one scheduled product – rice. Brazil

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[37] Panel Report, *Chile – PBS (21.5)*, paras. 7.141, 7.147, 7.152; Panel Report, *U.S. – Certain EC Products (21.5)*, para. 7.74; Panel Report, *EC – Bed Linen (21.5)*, para. 6.43.

[38] In *U.S. – Softwood Lumber VI (21.5)*, the Appellate Body concisely described this aspect of its conclusion in *EC – Bed Linen (21.5)* in the following terms: "a party cannot make the same claim of inconsistency against the same measure (or component of a measure) in an Article 21.5 proceeding if … the original panel found that the complaining party had not made out its claim with respect to the measure (or component of a measure (Appellate Body Report, *EC – Bed Linen (Article 21.5 – India)*, paras. 92-93 and 99)." Appellate Body Report, *U.S. – Softwood Lumber VI (21.5)*, para. 102 (note 150).

[39] Appellate Body Report, *EC – Bed Linen (21.5)*, para. 93 (emphasis in original). The original panel in that dispute stated that: "The issue before us is whether India should be allowed to raise, in this Article 21.5 proceeding, claims with respect to Article 3.5 which it **could and did** raise before the original panel, but which it did not pursue, and which the Panel dismissed for failure to present a *prima facie* case of violation." Panel Report, *EC – Bed Linen (21.5)*, para. 6.48 (emphasis in original). On review, the Appellate Body held that "the effect, for the parties, of findings adopted by the DSB as part of a panel report is the same, regardless of whether a panel found that the complainant failed to establish a *prima facie* case that the measure is inconsistent with WTO obligations, that the Panel found that the measure is fully consistent with WTO obligations, or that the Panel found that the measure is not consistent with WTO obligations." Appellate Body Report, *EC – Bed Linen (21.5)*, para. 96.

[40] Brazil's 16 January Submission, para. 12.

did not, as was the case for India in *EC – Bed Linen*, leave this finding unappealed. Rather, Brazil successfully appealed the original panel's finding. The Appellate Body reversed the original panel's finding that Brazil had failed to demonstrate actual circumvention with respect to pig meat and poultry meat, but was unable to complete the analysis given insufficient uncontested facts of record.[41]

45. The Appellate Body's reversal of the original panel's ruling, joined with its inability to complete the analysis, left the parties without final resolution of Brazil's claims regarding the provision of ECGs for exports of pig meat and poultry meat in excess of U.S. reduction commitments for those two products. This situation constitutes the effective equivalent of the exercise of false judicial economy, to which the Appellate Body also spoke in *EC – Bed Linen (21.5)*:

> The issue raised in this appeal is different from a situation where a panel, on *its* own initiative, exercises "judicial economy" by not ruling on the substance of a claim. … We believe that in a situation where a panel, in declining to rule on a certain claim, has provided only a partial resolution of the matter at issue, a complainant should not be held responsible for the panel's false exercise of judicial economy, such that a complainant would not be prevented from raising the claim in a subsequent proceeding.[42]

46. The circumstances in the present dispute are similar. The original panel erroneously excluded ECGs for pig meat and poultry meat from its findings regarding Brazil's circumvention claims. As a result of the original panel's failure to make the necessary factual findings, the Appellate Body, while reversing the original panel's conclusion as a matter of law, was unable to complete the analysis and offer Brazil satisfaction on its claims, through no fault of Brazil. In these circumstances, Brazil "should not be held responsible" for the lack of final resolution of its claims[43], and should be permitted, in these Article 21.5 proceedings, to renew its claims that the amended GSM 102 program has been applied to circumvent U.S. export subsidy commitments on pig meat and poultry meat.

47. In short, the circumstances that prevented India from renewing, in Article 21.5 proceedings in *EC – Bed Linen*, the same claim it had pursued in the original proceedings, are <u>not</u> present in the current dispute. Moreover, circumstances highlighted by the Appellate Body as not indicating final resolution of a claim <u>are</u> present in the current dispute.

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[41] Appellate Body Report, *U.S. – Upland Cotton*, paras. 689-694.

[42] Appellate Body Report, *EC – Bed Linen (21.5)*, para. 96 (note 115) (emphasis in original). In the past, the Appellate Body's use of the term "false judicial economy" has only been attached to an exercise of judicial economy that has been reversed on appeal. Thus, the Appellate Body's use of the phrase "false judicial economy" in *EC – Bed Linen (21.5)* suggests that in the circumstances it envisions, the complaining party will, in the original proceedings, have successfully appealed and secured reversal of that exercise of false judicial economy, therefore preserving its rights in the Article 21.5 proceedings. The compliance panel in *U.S. – OCTG Sunset Reviews (21.5)* faced a slightly different situation. In the Article 21.5 proceedings in that dispute, the compliance panel was asked whether an *unappealed* exercise of judicial economy in the original proceedings precludes review in Article 21.5 proceedings of the *same* claim raised with respect to a changed element of the measure. The compliance panel concluded that it did not:

> The fact that a panel, in an original dispute settlement proceeding, did not make findings [due to judicial economy] regarding certain issues relating to the investigating authorities' determination that were raised and argued before the panel, can not preclude a compliance panel, in its assessment under Article 21.5 of the DSU of the measures taken to comply with the DSB recommendations and rulings, from reviewing those aspects which have been incorporated by the authorities in the measure taken to comply."

Panel Report, *U.S. – OCTG Sunset Reviews (21.5)*, para. 7.92. This issue is currently on appeal. WT/DS268/19, para. 2.

[43] Appellate Body Report, *EC – Bed Linen (21.5)*, para. 96 (note 115) (emphasis in original).

48. In *U.S. – Shrimp (21.5)*, the Appellate Body similarly addressed limitations on the ability of a complaining Member to seek review, at the Article 21.5 phase, of the same claim addressed in the original proceedings. The Appellate Body concluded that a complaining Member can not pursue such a claim if it involved an unchanged aspect of the original measure that, in the original proceedings, had been found to be WTO-consistent.[44]

49. The situation confronted by the Appellate Body in *U.S. – Shrimp (21.5)* is different from the circumstances in the present dispute, for at least two reasons.[45]

50. First, in the original proceedings in the present dispute, the Appellate Body *reversed* the original panel's finding that Brazil had failed to demonstrate actual circumvention with respect to pig meat and poultry meat, but was unable to complete the analysis given insufficient uncontested facts of record.[46] There is, therefore, no finding of *WTO-consistency* with respect to Brazil's circumvention claims on pig meat and poultry meat, in stark contrast to the situation faced by the compliance panel and Appellate Body in *U.S. – Shrimp (21.5)*.

51. Second, as explained above, Brazil's claims of circumvention with respect to pig meat and poultry meat are not against an *unchanged aspect* of the same measure reviewed in the original proceedings. The measure subject to Brazil's claims, and the GSM 102-related "measures taken to comply" in this dispute, are the amendments to the GSM 102 fee schedule, and the amended GSM 102 program in its totality. Those measures taken to comply do not apply on a product-specific basis; in other words, the amended GSM 102 fee schedule makes no distinction between pig meat, poultry meat, other scheduled products, or unscheduled products.

52. The United States' attempt to *distinguish* the situation in the current Article 21.5 proceedings from relevant aspects of the second Article 21.5 proceedings in *Canada – Dairy* confirms the *similarity* between the two cases. As the United States notes, the United States and New Zealand requested a second Article 21.5 proceeding in *Canada – Dairy* "where the Appellate Body was unable to reach a decision in [an earlier proceeding] regarding the WTO-consistency of certain Canadian measure taken to comply because of a lack of sufficient facts."[47] That is precisely the situation in which Brazil finds itself. In the original proceedings, the Appellate Body reversed the original panel's finding that Brazil had failed to demonstrate actual circumvention with respect to pig meat and poultry meat, but was unable to complete the analysis given a lack of sufficient facts.[48]

53. While the United States possibly means to distinguish the two disputes with its observation that in *Canada – Dairy (21.5)*, the complaining Members' claims concerned "measures taken to comply", while in the present dispute, Brazil's claims do not, Brazil has already demonstrated that its claims are indeed with respect to a "measure taken to comply".

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[44] Appellate Body Report, *U.S. – Shrimp (21.5)*, paras. 89, 96 ("89. ... Malaysia seems to suggest ... that a panel must re-examine, for WTO-consistency, even those aspects of a new measure that were part of a previous measure that was the subject of a dispute, and were found by the Appellate Body to be WTO-consistent in that dispute, and that remain unchanged as a part of the new measure. .... 96. [T]he Panel ... rightly concluded that our ruling in *United States – Shrimp* with respect to the consistency of [the unchanged aspect of the measure], therefore, still stands").

[45] In *U.S. – Softwood Lumber VI (21.5)*, the Appellate Body concisely described this aspect of its conclusion in *U.S. – Shrimp (21.5)* in the following terms: "a party cannot make the same claim of inconsistency against the same measure (or component of a measure) in an Article 21.5 proceeding if the original panel and Appellate Body found the measure to be consistent with the obligation at issue (Appellate Body Report, *U.S. – Shrimp (Article 21.5 – Malaysia)*, paras. 89-99) ...." Appellate Body Report, *U.S. – Softwood Lumber VI (21.5)*, para. 102 (note 150).

[46] Appellate Body Report, *U.S. – Upland Cotton*, paras. 689-694.

[47] U.S. Rebuttal Submission, para. 13 (note 19).

[48] Appellate Body Report, *U.S. – Upland Cotton*, paras. 689-694.

54. Finally, a further reason that the circumstances of this dispute differ from those in *EC – Bed Linen (21.5)* and *U.S. – Shrimp (21.5)* is that Brazil's claims do not concern an *unchanged* aspect of the original measure. Rather, as noted, Brazil's claims concern the *changed* guarantee fee schedule of the amended GSM 102 program.

c. Interpretive bases for limits on claims

55. Based on the jurisprudence, Brazil has demonstrated that its claims of circumvention with respect to pig meat and poultry meat are legitimately within the scope of these Article 21.5 proceedings. To respond to part (a) of the compliance Panel's question, Brazil now reviews the interpretive basis for the various limitations on the right of a complaining Member to assert particular claims in Article 21.5 proceedings.

56. First, Brazil addresses the interpretive basis for the limits on new claims discussed above. According to panels, allowing any and all new claims in expedited compliance proceedings, without imposition of the limits discussed above in respect of an unchanged aspect of the original measure, would jeopardize the "security and predictability" of the WTO dispute settlement system, in contravention of Article 3.2 of the DSU[49], and the principles of fundamental fairness and due process inherent to dispute settlement[50], as well as the object and purpose of Article 21.5.[51]

57. Second, Brazil addresses the interpretive basis for the limits discussed above on the ability of a complaining Member to bring the same claim it had pursued in the original proceedings regarding an unchanged aspect of the original measure. The interpretive basis for these limits is somewhat richer, and is based on reading Article 21.5 in the context of Articles 16.4, 19.1, 21.1, 21.3 and 22.1 of the DSU. The Appellate Body's interpretation is best developed in its report in *EC – Bed Linen (21.5)*:

> Where a panel concludes that a measure is inconsistent with a covered agreement, that panel shall *recommend*, according to Article 19.1, that the Member concerned bring that measure into conformity with that agreement. A panel report, including the *recommendations* contained therein, shall be *adopted* by the DSB within the time period specified in Article 16.4 – unless appealed. Members are to *comply* with recommendations and rulings *adopted* by the DSB promptly, or within a reasonable period of time, in accordance with paragraphs 1 and 3 of Article 21 of the DSU. A Member that does not comply with the recommendations and rulings adopted by the DSB within these time periods must face the consequences set out in Article 22.1, relating to compensation and suspension of concessions. Thus, a reading of Articles 16.4 and 19.1, paragraphs 1 and 3 of Article 21, and Article 22.1, taken together, makes it abundantly clear that a panel finding which is not appealed, and which is included in a panel report *adopted* by the DSB, must be accepted by the parties as a *final* resolution to the dispute between them, in the same way and with the same finality as a finding included in an Appellate Body Report adopted by the DSB – with respect to the particular claim and the specific component of the measure that is the subject of the claim.[52]

58. These interpretive elements do not bar the compliance Panel from considering Brazil's claims of circumvention with respect to pig meat and poultry meat. As observed above, Brazil's claims relate to the changed guarantee fee schedule of the amended GSM 102 program, which is not an unchanged aspect of the original measure. Brazil's claims also do not involve a panel finding that was "not

[49] Panel Report, *Chile – PBS (21.5)*, para. 7.152.
[50] Panel Report, *U.S. – Certain EC Products (21.5)*, para. 7.75
[51] Panel Report, *EC – Bed Linen (21.5)*, para. 6.43.
[52] Appellate Body Report, *EC – Bed Linen (21.5)*, para. 93 (emphasis in original).

appealed", that was "included in a panel report *adopted* by the DSB", and that must therefore, as a result of Articles 16.4, 19.1, 21.1, 21.3 and 22.1 of the DSU, be accepted by Brazil "as a *final* resolution" of the claim.

59. As support for its conclusion on the limits announced in *EC – Bed Linen (21.5)*, the Appellate Body also referred to the object and purpose of the DSU, noting that

> Article 3.3 provides that the *prompt* settlement of disputes is "essential to the effective functioning of the WTO". Article 21.5 advances the purpose of achieving a prompt settlement of disputes by providing an expeditious procedure to establish whether a Member has fully complied with the recommendations and rulings of the DSB. For that purpose, an Article 21.5 panel is to complete its work within 90 days, whereas a panel in an original dispute is to complete its work within 9 months of its establishment, or within 6 months of its composition. It would be incompatible with the function and purpose of the WTO dispute settlement system if a claim could be reasserted in Article 21.5 proceedings after the original panel or the Appellate Body has made a finding that the challenged aspect of the original measure is *not* inconsistent with WTO obligations, and that report has been adopted by the DSB. At some point, disputes must be viewed as definitely *settled* by the WTO dispute settlement system.[53]

60. These interpretive elements do not bar the compliance Panel from considering Brazil's claims of circumvention with respect to pig meat and poultry meat. As observed above, Brazil's claims do not involve reassertion of the same claim in Article 21.5 proceedings regarding an unchanged aspect of the original measure, following a finding by the original panel or the Appellate Body "that the challenged aspect of the original measure is *not* inconsistent with WTO obligations"; indeed, the Appellate Body reversed the original panel's finding that the ECG programs with respect to pig meat and poultry meat were not inconsistent with the export subsidy provisions of the *Agreement on Agriculture* and the *SCM Agreement*.

E. Conclusion

61. In its response to this question, Brazil has demonstrated that the measures and claims subject to the United States' ECG-related request for preliminary ruling pertain to a "measure taken to comply". Specifically, Brazil has demonstrated that its challenge relates to a new aspect of a new measure – the modified fee schedule that is part of the amended GSM 102 program. Brazil's answer demonstrates that in these circumstances, its challenge adheres to the textual and jurisprudential limits on the measures that may properly be challenged in Article 21.5 proceedings.

62. Separately, Brazil has demonstrated that in these proceedings, it is raising the same claims that it raised in the original proceedings, with respect to this new aspect of a new measure. Specifically, Brazil has demonstrated that its claims relate to the application of the amended GSM 102 to circumvent U.S. export subsidy commitments on pig meat and poultry meat; in the original proceedings, Brazil similarly claimed that the old GSM 102 was applied to circumvent U.S. export subsidy commitments on these two products. No final resolution was achieved, even with respect to this now-changed aspect of the old measure. Brazil's answer demonstrates that in these circumstances, its challenge adheres to the textual and jurisprudential limits on the claims that may properly be subject to review under Article 21.5.

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[53] Appellate Body Report, *EC – Bed Linen (21.5)*, para. 98 (emphasis in original). *See also* Panel Report, *Chile – PBS (21.5)*, para. 7.135.

Questions to Brazil

7. Is Brazil of the view that it is only in the circumstances identified by the Appellate Body in EC – Bed Linen (Article 21.5 – India) that the scope of Article 21.5 proceedings is limited by the scope of the original proceedings? [Paragraphs 11-15 of Submission of Brazil to the Panel Regarding US Requests for Preliminary Ruling]

63. No. As discussed in Brazil's response to question 6, panels and the Appellate Body have addressed a number of circumstances in which the scope of Article 21.5 proceedings is limited by the scope of the original proceedings. None of these apply to Brazil's claims regarding the modified guarantee fee schedule of the amended GSM 102 program.

8. How does Brazil respond to the arguments of the United States that Brazil "incorrectly assumes that the standard is one of whether there has been a 'final resolution' of the issue in the original proceeding" and that Brazil misreads the Appellate Body report in EC – Bed Linen (Article 21.5 – India) and confuses the issue of "the scope of a compliance proceeding pursuant to Article 21.5 of the DSU" and the distinct issue of "when a claim against a specific measure or aspect of a measure can be considered to be 'finally resolved' for purposes of WTO dispute settlement"? [Paragraphs 8 and 12 of the Rebuttal Submission of the United States]

64. Brazil agrees that assessing the proper scope of an Article 21.5 proceeding requires separate determinations that (i) the measure at issue is a "measure taken to comply", and (ii) the claims levied by the complaining Member with respect to that measure are subject to review in compliance proceedings.

65. In its submissions to the compliance Panel, the United States does not appear to challenge the "final resolution" standard *per se*, as a means of assessing the question in part (ii). That is, the basis for the United States' preliminary objection is not that Brazil is prohibited from pursuing the same claims that it maintained in the original proceedings, where there has not been final resolution of those claims.

66. Rather, as discussed in Brazil's response to question 6, the United States' ECG-related request for preliminary ruling concerns solely part (i) of the assessment. Specifically, the United States argues that Brazil is prohibited from pursuing those same claims in these Article 21.5 proceedings, because the claims concern a measure that is allegedly not a "measure taken to comply". In its response to question 6, Brazil has demonstrated that its claims do indeed concern a "measure taken to comply".

9. What are the comments of Brazil on the arguments in footnote 22 of the United States' rebuttal submission?

67. Brazil's first comment is that the United States has never addressed the fact that Brazil's claims in this dispute pertain to the *modified guarantee fee schedule* of the *amended* GSM 102 program. Thus, the limitations in Article 21.5 on raising claims in compliance proceedings regarding an *unchanged* aspect of the *original* measure do not apply.

68. There are several arguments raised by the United States in footnote 22 of its Rebuttal Submission.

69. The United States appears to argue, **first**, that where the Appellate Body has reversed an original panel's finding of WTO-inconsistency with respect to a particular claim, but found itself

unable to complete the analysis given a lack of sufficient facts, that claim can not be considered by a compliance panel in subsequent proceedings.[54]

70. The U.S. argument is inconsistent with *EC – Bed Linen (21.5)*[55], in which the Appellate Body concluded that the exercise of judicial economy with respect to a claim raised in the original proceedings does not bar a complaining Member from reasserting that same claim in Article 21.5 proceedings.[56]

71. In some respects, the situation in the current dispute is the effective equivalent of the exercise of judicial economy described by the Appellate Body as presenting no bar to consideration of a claim in subsequent Article 21.5 proceedings. The original panel erroneously excluded ECGs for pig meat and poultry meat from its findings regarding Brazil's circumvention claims. As a result of the original panel's failure to make the necessary factual findings, the Appellate Body, while reversing the original panel's conclusion as a matter of law, was unable to complete the analysis and offer Brazil satisfaction on its claims, through no fault of Brazil. In these circumstances, Brazil "should not be held responsible" for the lack of final resolution of its claims regarding the *original* measure[57], and should be permitted, in these Article 21.5 proceedings, to renew its claims that the *amended* GSM 102 program has been applied to circumvent U.S. export subsidy commitments on pig meat and poultry meat.

72. **Second**, implicit in the United States' argument is an assertion that "the measures" subject to Brazil's claims remain unchanged from the original proceedings. As demonstrated in response to questions 6 and 8, however, Brazil's ECG-related claims of inconsistency with the covered agreements do indeed involve a new "measure taken to comply" and, in particular, the modified guarantee fee schedule in that new measure. The measure subject to Brazil's claims is a "measure taken to comply" – the GSM 102 program as amended by the modified GSM 102 fee schedule.

73. **Third**, in arguing that "Brazil would have this compliance Panel assume that the Appellate Body *had* made a finding of WTO-inconsistency with respect to the pig meat and poultry meat GSM 102 guarantees and *had* made a recommendation that the United States bring these measures into compliance,"[58] the United States reveals a misunderstanding of the compliance Panel's task. The Appellate Body has clarified that the task of a compliance panel operating under Article 21.5 is not limited to the issue whether the defending Member has implemented the recommendations of the DSB.[59] Instead, the compliance Panel must examine whether the *revised* measure is consistent with all of the implementing Member's WTO obligations – including the United States' export subsidy commitments for pig meat and poultry meat.

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[54] U.S. Rebuttal Submission, para. 14 (note 22) ("Brazil is effectively asking the Panel to render meaningless the fact that the Appellate Body *declined* to make any finding of WTO-inconsistency with respect to the measures because it *did not* find uncontested facts showing that the measures were provided inconsistently with any U.S. WTO obligations. Brazil would have this Panel assume that the Appellate Body *had* made a finding of WTO-inconsistency with respect to the pig meat and poultry meat GSM 102 guarantees and *had* made a recommendation that the United States bring these measures into compliance with the obligations assumed to be breach [sic] (and further to assume that this recommendation was adopted by the DSB). None of these things happened, and Brazil has no basis for asking the Panel to pretend otherwise.").

[55] As described in Brazil's response to question 6, the U.S. argument would similarly have prevented it from bringing the claims asserted in the second Article 21.5 proceeding in *Canada – Dairy*.

[56] Appellate Body Report, *EC – Bed Linen (21.5)*, para. 96 (note 115). *See also* Panel Report, *U.S. – OCTG Sunset Reviews (21.5)*, para. 7.92 (currently on appeal).

[57] Appellate Body Report, *EC – Bed Linen (21.5)*, para. 96 (note 115) (emphasis in original).

[58] U.S. Rebuttal Submission, para. 14 (note 22).

[59] *See, e.g.*, Appellate Body Report, *Canada – Aircraft (21.5)*, paras. 40-41. *See also* Panel Report, *Chile – PBS (21.5)*, paras. 7.136-7.137.

74. **Fourth**, and finally, the United States argues that, if Brazil is permitted to pursue its claim against U.S. use of the amended GSM 102 program to circumvent U.S. export subsidy commitments for pig meat and poultry meat, in the absence of a finding by the original panel or the Appellate Body of circumvention with respect to pig meat and poultry meat, and in the consequent absence of a DSB recommendation concerning circumvention with respect to pig meat and poultry meat, the United States could be "deprived of a reasonable period of time to bring any measures found to be WTO-inconsistent into compliance with its obligations", "where a measure (that is not a measure taken to comply) is found to be WTO-inconsistent for the first time in an Article 21.5 proceeding."[60]

75. The underlined portion of this statement reveals the fundamental error in the United States' reasoning. As demonstrated in response to questions 6 and 8, Brazil's ECG-related claims of inconsistency with the covered agreements do indeed involve a "measure taken to comply". The measure subject to Brazil's claims is the "measure taken to comply" – the GSM 102 program as amended by the modified GSM 102 fee schedule.

76. For systemic reasons, Brazil would like to address the relevance of the potential "deprivation" highlighted by the United States, assuming that the measure at issue is a "measure taken to comply" (and, thus, assuming that the underlined parenthetical is stricken from the United States' statement).

77. In that case, the potential "deprivation" noted by the United States is inherent to the Article 21.5 process. Where a Member adopts a "measure taken to comply", it is subject to review, under the expedited procedures of Article 21.5, for "consistency with a covered agreement". The text of Article 21.5 does not specify that consistency must be judged with reference to the particular provisions of the particular covered agreement under which a violation was found in the original proceedings. As noted above, the compliance Panel's mandate is to review the consistency of the measure with the covered agreements, and not with the specific recommendations made by the DSB.

78. If the Member's "measure taken to comply" is found to be WTO-inconsistent, the Member is not accorded an additional "reasonable period of time" to bring its measure into compliance. This has been confirmed by the Appellate Body and the compliance panel in *U.S. – FSC (21.5 II)*, another dispute involving recommendations under Article 4.7 of the *SCM Agreement*. The Appellate Body noted that if findings of violation in Article 21.5 proceedings "were to result in an extension of the time period set for" compliance,

> compliance proceedings could have the effect of extending implementation periods … in successive Article 21.5 proceedings. This could lead to a potentially "never-ending cycle" of dispute settlement proceedings and inordinate delays in the implementation of recommendations and rulings of the DSB.[61]

79. The compliance panel in that dispute in fact noted a problem that the United States ignores – allowing Members to secure additional time to implement recommendations through the Article 21.5 process would give them an incentive to adopt non-compliant "measures taken to comply":

> Nowhere do we find any indication in the text or context of Article 21.1/21.5 of the *DSU* or of Article 4.7 of the *SCM Agreement*, nor in the object or purpose of the *DSU* (nor, for that matter, the *SCM Agreement*) that would require repeated extensions of the implementation period in Article 21.5 *DSU* compliance proceedings. Indeed, such an interpretation would reduce the textual treaty terms "prompt compliance" and "without delay" to redundancy and inutility. We are not permitted to adopt such an

[60] U.S. Rebuttal Submission, para. 14 (note 22) (emphasis added).
[61] Appellate Body Report, *U.S. – FSC (21.5 II)*, para. 86, *quoting* Panel Report, *U.S. – FSC (21.5 II)*, para. 7.46.

> interpretation. Such an approach might lead to a potentially never-ending cycle, whereby a Member continues to adopt non-compliant measures in order to win more time to comply with adopted DSB recommendations and rulings. This would entirely undermine the effective operation of the WTO dispute settlement system.[62]

80. The potential "deprivation" of which the United States speaks is not unique to the current Article 21.5 proceeding; it is inherent to Article 21.5 proceedings generally, and is why it is incumbent on a defending Member, having already been found to be in violation of its WTO obligations, to adopt "measures taken to comply" that are fully WTO-consistent. No more time for implementation is, or should be, accorded. Having already been found to be in violation of its WTO obligations, the defending Member's curative "measures taken to comply" violate its obligations and commitments at its peril. As noted by the compliance panel in *U.S. – FSC (21.5)*,

> Article 21.5 comes after the "recommendation" provision in Article 19 of the *DSU*, and the principle of "prompt compliance" in Article 21.1, as part of the WTO dispute settlement process. The title of Article 21 – "Surveillance of recommendations and rulings" – is telling. It informs us that the proceedings are to follow the implementation of recommendations and rulings that have been made. This finds further support in the particular nature and purpose of *compliance* panel proceedings.[63]

81. Using the Article 21.5 process to "add[] to the 'non-implementing' Member's rights under the covered agreements through an extension of the time-period for implementation" would undermine the object and purpose of compliance proceedings.[64]

82. The rights and obligations of complaining and defending Members in Article 21.5 proceedings are finely balanced. The potential "deprivation" noted by the United States is a burden a defending Member in an Article 21.5 proceedings must bear, as a result of the terms of Article 21.5 and the object and purpose of compliance proceedings. Similarly, Brazil has described in detail (in its response to question 6) the limits imposed on complaining Members in Article 21.5 disputes – they may challenge only "measures taken to comply", and they may pursue only those claims not yet subject to final resolution.

Question to the US

10. Could the United States explain why it considers that what it describes as the "final resolution" standard is not the correct standard to decide whether Brazil's claims regarding export credit guarantees for pig meat and poultry meat are within the scope of this proceeding?

2. Preliminary objections of the United States with respect to claims of Brazil regarding marketing loan and counter-cyclical payment programs

Questions to Brazil

11. Is Brazil of the view that a finding under Article 6 of the SCM Agreement that a "subsidy" is causing serious prejudice necessarily always applies to both the subsidy "payments" and the subsidy "program"? [Paragraphs 31-35 of Submission of Brazil Regarding US Requests for Preliminary Ruling and paragraph 38 of the Rebuttal Submission of Brazil]

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[62] Panel Report, *U.S. – FSC (21.5 II)*, para. 7.46 (emphasis added).
[63] Panel Report, *U.S. – FSC (21.5 II)*, para. 7.42.
[64] Panel Report, *U.S. – FSC (21.5 II)*, para. 7.45.

83. Brazil considers that the answer to this question depends on the particular facts before a panel. Brazil recognizes that there might be situations where a Member makes subsidy "payments" in the absence of a subsidy "program". In that case, a finding of serious prejudice could be made regarding payments alone. However, if a Member challenges "payments" that are mandated by a program, a finding regarding the payments necessarily implicates the program.

84. There may also be situations where a Member challenges subsidy "programs". In that event, a finding of serious prejudice necessarily applies to payments mandated under the program. When a subsidy program mandates certain subsidy payments, an examination of the "*effects*" of the program necessarily includes an assessment of the circumstances in which mandatory payments are made; the nature of those payments, including their general amount and the intended recipients; and the impact of those payments in the marketplace. In short, the WTO-consistency of a program under Article 6 of the *SCM Agreement* cannot be artificially separated from the WTO-consistency of payments mandated by a program.

85. Turning to the specific facts of this case, in the original proceedings, Brazil challenged both the subsidy "programs" and the subsidy "payments" mandated under those programs. As a result, the original panel's findings under Article 6 apply to both. This is confirmed by the original panel's description of the contested measures; its examination of those measures; and its conclusion that those measures cause serious prejudice.

86. The original panel's findings regarding its terms of reference illustrate that the contested measures found to be WTO-inconsistent included the subsidy programs in the FSRI Act of 2002 and the payments mandated by them. The United States contended that the panel's terms of reference excluded payments made after the date of the panel's establishment. The original panel rejected this argument, stressing that:

> The *programs and legislation* identified [in Brazil's request for establishment of a panel] *include payments* made before the date of establishment of the Panel, *and those made subsequently*. *All such payments were and are made under the same legislative and regulatory provisions which entered into effect prior to the consultations and have remained in place throughout the Panel proceeding. Therefore, the Panel rules that payments under programs and legislation within the Panel's terms of reference, made after the date on which the Panel was established … are within its terms of reference*.[65]

87. The original panel, therefore, found that the contested measures included "*programs and legislation*" identified in the panel request, together with "*payments*" made under the contested programs *at any time during the panel proceedings.* Thus, the original panel viewed the mandatory payments as intrinsic to the contested programs, and as part of its terms of reference. Nothing in this finding suggests that the original panel artificially separated the subsidy programs from mandatory payments made pursuant to those programs. Further, the original panel stated no temporal limitations on the subsidy measures examined. The United States did not appeal these findings.

88. In making this finding, the original panel opined that it would undermine the object and purpose of the *SCM Agreement* if a Member were unable to challenge subsidies "until they were actually paid".[66] The panel, therefore, had in mind that a subsidy program mandating payments could cause adverse effects, even before payments are disbursed. In this regard, the original panel found

[65] Panel Report, *U.S. – Upland Cotton*, para. 7.187.
[66] Panel Report, *U.S. – Upland Cotton*, para. 7.191.

that "it is clear that the existing subsidy programs are currently envisaged to remain in effect between MY 2003-MY 2007."[67]

89. Having found that its terms of reference encompassed the subsidy programs and past, present and future payments mandated by those programs, the original panel also stated expressly, in paragraph 7.1107 of its report, that the measures at issue in Brazil's "present" serious prejudice included the "*legislative and regulatory provisions currently providing*" for marketing loan, CCP, and Step 2 payments, as well as the "payments" mandated by those legislative and regulatory provisions.[68] Again, the original panel stated no general temporal limitation on the scope of the measures and, again, these findings were not appealed by the United States.

90. Significantly, the original panel noted that the measures involved in Brazil's present serious prejudice claims included cottonseed payments *limited to* the "2000 crop".[69] This is a clear temporal limitation on a subsidy measure. Thus, any findings by the original panel would have been restricted to the effects of cottonseed payments made in MY 2000.[70] However, no such temporal limitation is placed on any of the other measures listed in paragraph 7.1107.[71]

91. Immediately after listing the "legislative and regulatory provisions" as measures that were part of the present serious prejudice analysis, the original panel cross-referenced to Brazil's "per se" claims. It used the phrase "*see also* Brazil's *per se* actionable subsidy claims in Section VII:I."[72] Contrary to the U.S. argument, this cross-reference, and the use of the word "also", confirms that the "legislative and regulatory provisions" of the FSRI Act of 2002 were included in the present serious prejudice analysis and "also" in the *per se* claims.

92. The original panel then chose a "reference period" for assessing the effects of the contested subsidy programs and mandatory payments. Although the original panel chose MY 2002 as an appropriate "reference period", it declared that it would be "inappropriate" to focus its analysis on MY 2002 alone. It found that subsidies have been provided "over a longer period of time than one year" and that consideration of developments over a period longer provided a more robust basis for its conclusion.[73] The original panel, therefore, sought to put the effects of the contested subsidy programs into "a broader temporal context".[74] This is also consistent with the fact that its terms of reference extended to mandatory payments made throughout the panel proceedings.

93. Thus, the choice of MY 2002 served as a *methodological tool* to marshal and examine evidence relating to the "effects" of the contested subsidy programs. Moreover, the original panel's use of that tool was not exhaustive, but was complemented by an examination of data from other periods. Also, in selecting a "reference period", the panel did not make a jurisdictional decision that the measures at issue were limited to payments within the "reference period". Indeed, any such finding would have contradicted the panel's conclusion that the measures at issue included the "legislative and regulatory provisions" establishing the subsidy programs, as well as all payments made under these programs "throughout the Panel proceeding".[75]

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[67] Panel Report, *U.S. – Upland Cotton*, para. 7.1500.
[68] Panel Report, *U.S. – Upland Cotton*, paras, 7.1107.
[69] Panel Report, *U.S. – Upland Cotton*, para. 7.1107(viii).
[70] The original panel did not find that cottonseed payments caused significant price suppression.
[71] Further, Brazil has explained in its answer to Question 11 that the panel's cross-reference using the phrase "see **also** Brazil's per se actionable subsidy claims in Section VII:1" confirms that the panel examined both the payments and programs in making its present serious prejudice findings.
[72] Panel Report, *U.S. – Upland Cotton*, para. 7.1107, note 1247.
[73] Panel Report, *U.S. – Upland Cotton*, para. 7.1199.
[74] Panel Report, *U.S. – Upland Cotton*, para. 7.1199.
[75] Panel Report, *U.S. – Upland Cotton*, para. 7.187.

94. The United States' contention that the original panel's findings were confined to "payments" is further contradicted by that panel's treatment of "payments" in its reasoning. The United States tried, but failed, to demonstrate that Brazil was required to quantify precisely the amount of the payments made.[76] The original panel dismissed these arguments, holding that there was no duty to quantify the amount of the payments nor to trace payments to particular recipients and/or products.[77]

95. Instead, the original panel undertook an analysis of the "effects" of the contested subsidy programs by focusing on their "*structure, design and operation*".[78] It stated that this "*qualitative*" analysis was to be complemented, "to some extent", by a "quantitative analysis" of the "general order of magnitude of the subsidies" (*i.e.*, the general level of payments).[79] The Appellate Body bolstered this qualitative aspect of the original panel's approach, noting the importance of the "*nature* of the subsidy" to an assessment of the subsidy's effects under Article 6 of the *SCM Agreement*.[80]

96. If the original panel's findings had related to "payments" alone, and not to the subsidy programs, its reasoning would have been very different indeed. The panel would have required precise identification of the contested subsidy payments, including their amount, and the recipients and products receiving them, because these would have been the measures at issue. A precise quantitative examination of the magnitude of "payments" would have been of central importance and not merely conducted "to some extent", as a complement to the qualitative examination. Moreover, the *qualitative* examination of the "structure, design and operation" of the measures would have been meaningless because the dollar amount of payments do not have "structure", "design" or "operation".

97. The focus by the original panel on "programs" in its present serious prejudice analysis is illustrated in its finding that the price suppression in the world market was "significant." It reasoned as follows:

> During the period under consideration, given the relative magnitude of United States production and exports, the overall price trends we identified in the world market, and *the nature of the mandatory United States subsidies in question – in particular, the market-price contingent, countercyclical, nature of the marketing loan program, the user marketing (Step 2) program, MLA payments, and CCP payments* - and the readily available evidence of the order of magnitude of the subsidies, we are certainly not, by any means, looking at an insignificant or unimportant world price phenomenon.[81]

98. This is a crucial finding because it was the basis for the determination that the amount of price suppression in the world market was high enough to cause a violation of Article 6.3(c) ("significant" price suppression). And the *nature* of the *mandatory, price-contingent* marketing loan *program* was a vital factor in the original panel's finding. The passage shows, again, that the subsidy measures found by the original panel to be WTO-inconsistent included "*mandatory*" subsidy "*programs*", and not just

[76] Panel Report, *U.S. – Upland Cotton*, paras 7.1159-7.1174.
[77] Panel Report, *U.S. – Upland Cotton*, para. 7.1173.
[78] Panel Report, *U.S. – Upland Cotton*, para 7.1194.
[79] Panel Report, *U.S. – Upland Cotton*, para 7.1173; *see also* Appellate Body Report, *U.S. – Upland Cotton*, para. 467 ("a panel should have regard to the magnitude of the challenged subsidy *and its relationship to prices of the product in the relevant market* when analyzing whether the effect of a subsidy is significant price suppression"; the issue of when prices are low enough to trigger the subsidies is part of the design and operation of the subsidy program set out in a legislative and regulatory framework).
[80] Appellate Body Report, *U.S. – Upland Cotton*, para. 450 ("The nature of a subsidy plays an important role in any analysis of whether the effect of the subsidy is significant price suppression under Article 6.3(c).").
[81] Panel Report, *U.S. – Upland Cotton*, para. 7.1332 (emphasis added).

"payments". These findings were also consistent with extensive evidence of the price suppressing effects of the price-contingent "programs" presented by Brazil to the original panel.[82]

99. Given all of these findings, it is of no surprise that in describing its conclusions on present serious prejudice, the original panel confirmed that the WTO-inconsistent measures causing serious prejudice included the "present statutory and regulatory framework" of the FSRI Act of 2002:

> Because the Panel's "present" serious prejudice findings include findings of inconsistency that deal with the FSRI Act of 2002 and subsidies granted thereunder in MY 2002, the United States is obliged to take action concerning its present statutory and regulatory framework as a result of our "present" serious prejudice finding. We recall that, pursuant to Article 7.8 of the *SCM Agreement*, the United States is under an obligation to "take appropriate steps to remove the adverse effects or ... withdraw the subsidy.[83]

100. In paragraph 7.1503 of its report, the original panel confirmed that, during implementation, the United States was required to "*significantly transform[]*" the contested subsidy programs such that, after implementation, any subsidy programs maintained by the United States would be "*manifestly different*" from those originally contested. The United States never appealed these findings.

101. These findings were crucial to the original panel's decision that there was no need for the original panel to address Brazil's claims of threat of serious prejudice. The original panel noted that Brazil's threat claims extended throughout "the remaining period of application of the FSRI Act of 2002"; that is, through MY 2007.[84] Because the United States was obliged by the present serious prejudice findings to "significantly transform" the "present statutory and regulatory framework" of the FSRI Act of 2002, there was no need for the panel to consider a threat of serious prejudice through MY 2007.

102. Thus, the original panel held that the United States was obliged to take action to modify, or withdraw, the contested subsidy programs to eliminate present serious prejudice that would otherwise persist throughout "the remaining period of application of the FSRI Act of 2002".[85] On any other view, the original panel would have examined Brazil's claims of a threat of serious prejudice in MY 2007.

103. This is also confirmed by paragraph 8.1(g)(i) of the original panel report, in which the panel concludes that "*mandatory price-contingent* United States subsidy *measures*" are inconsistent with Article 5(c) and 6.3(c) of the *SCM Agreement*. The reference to "mandatory price-contingent" measures refers to the contested subsidy *programs* that mandate payments on price-contingent basis. This expression does not encompass payments of specific dollar amounts made during a defined period of time because the payments do not mandate anything.

104. Thus, the original panel's description of the measures, its reasoning regarding present and threat of serious prejudice, and its conclusions, demonstrate that the measures found to be causing significant price suppression in the world market included the "statutory and regulatory framework" establishing the subsidy programs, as well as the continual flow payments mandated under these programs year after year through until MY 2007.

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[82] Brazil Submission Regarding the U.S. Request for Preliminary Ruling, para. 38, note 47.
[83] Panel Report, *U.S. – Upland Cotton*, para. 7.1501.
[84] Panel Report, *U.S. – Upland Cotton*, para. 7.1500.
[85] Panel Report, *U.S. – Upland Cotton*, para. 7.1500.

105. Thus, given the original panel's finding in paragraph 7.1501, any "appropriate steps" that the United States was obligated to take must have included changes to its "present statutory and regulatory framework".

106. Indeed, the United States took one such "statutory and regulatory" step (albeit insufficient). Brazil has observed that statements by the United States on the significance of the repeal of the Step 2 program – itself set forth in the FSRI Act of 2002 – demonstrate that the United States itself considered that it was required "to take action concerning its present statutory and regulatory framework as a result of our 'present' serious prejudice finding."[86] In August 2006, a USTR spokeswoman, Gretchen Hamil, stated that "repeal of the Step 2 program ... addresses [the] ... actionable subsidy findings in the dispute."[87] The U.S. Department of Agriculture also stated that the "legislative action" to repeal the Step 2 program "addresses a WTO finding regarding suppression of world cotton prices."[88]

107. It is only in these compliance proceedings that the United States has, for the first time, espoused the view that compliance required it to take no action whatsoever to change the contested subsidy programs, and instead permitted it to eliminate the effects of "payments" by payments of billions more dollars under the very same programs.

108. In conclusion, the compliance Panel inquired whether a finding under Article 6 of the *SCM Agreement* always necessarily applies to subsidy "payments" and subsidy "programs". As observed in Brazil's response, there might be situations in which a Member makes subsidy "payments" in the absence of a subsidy "program"; in that case, a finding of serious prejudice could be made regarding subsidy "payments" alone. However, Brazil has demonstrated above that in this dispute, the findings of the original panel applied to both subsidy "payments" and subsidy "programs".

12. In paragraph 44 of its Rebuttal Submission, Brazil states:

> ***"Accordingly, there is no need for Brazil to challenge per se the FSRI Act of 2002. Nor does it assert an 'as applied' challenge to the FSRI Act of 2002. Rather, Brazil challenges the counter-cyclical and marketing loan programs in the FSRI Act of 2002 and the payments that such programs require to U.S. upland cotton farmers, as they cause adverse effects." (emphasis added)***

Could Brazil please explain:

> ***a) How its claims against "programs and payments... as they cause adverse effects" differ from claims against programs as such?***

109. As explained in reply to Question 11, in the context of claims regarding the "effects" of subsidy programs that mandate subsidy payments, Brazil does not see any practical difference between challenging the programs and payments, and challenging the programs as such. Nor does Brazil see any difference in terms of a finding that the United States has not complied with Article 7.8 of the *SCM Agreement.*

110. Brazil's request for establishment of a panel in this Article 21.5 proceeding identifies the contested measures as the marketing loan and counter-cyclical "programs" and the marketing loan and counter-cyclical "payments." The use of the terms "program" and "payments" describes collectively

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[86] Panel Report, *U.S. – Upland Cotton*, para. 7.1501.

[87] Exhibit Bra-438 *(*"U.S. Trade Officials Say Disappointed With Brazil's WTO Request Over Cotton Flap," Daily Report for Executives, 21 August 2006).

[88] Exhibit Bra-436 (Cotton and Wool Outlook, USDA, 13 March 2006, p. 4, accessed October 2006 at http://usda.mannlib.cornell.edu/usda/ers/CWS//2000s/2006/CWS-03-13-2006.pdf).

the "subsidy" measures involved in this dispute. Brazil's claims relate to the effects of the marketing loan and counter-cyclical subsidy programs and the payments mandated by those programs.

111. Brazil has demonstrated that these two subsidy programs, and the payments they mandate, cause significant price suppression in the world market for upland cotton as well as an increase in the U.S. world market share of upland cotton in MY 2005. The evidence and arguments set forth by Brazil establishes that the United States has failed to take appropriate steps to either withdraw the marketing loan and counter-cyclical subsidies or to remove the adverse effects caused by these subsidies.

112. While Brazil has challenged the marketing loan and counter-cyclical "programs" and their mandatory, price-contingent "payments", to the extent they cause adverse effects, it has not asserted an "as such" claim regarding the marketing loan and counter-cyclical payment programs in the FSRI Act of 2002. As explained in reply to Question 11, if Brazil had made such a claim (which Brazil believes is unnecessary in view of the original panel's findings), the compliance Panel's examination of the "*effects*" of the program would necessarily have included an assessment of the terms and conditions under which payments are mandated; the nature of those payments, including their general amount, and the intended recipients and/or products benefiting from them; and the impact (or "effect") of those payments in the marketplace.

113. If Brazil's "as such" claim had been successful, the result would be a finding by the compliance Panel that the United States failed to take appropriate steps, pursuant to Article 7.8 of the *SCM Agreement* to withdraw the marketing loan and counter-cyclical subsidies, or to remove the adverse effects caused by these subsidies. Therefore, the ultimate conclusion of this compliance Panel would be the same whether the compliance Panel were to find that the "subsidies" cause present serious prejudice, or whether the marketing loan and counter-cyclical payment "program" is "as such" inconsistent with the *SCM Agreement*.

114. Finally, Brazil agrees with the United States' observation in *EC – Selected Customs Matters* that certain claims under the covered agreements are "not readily classifiable in the categories of 'as such' and 'as applied.'"[89] An "as such" claim is typically understood to involve an examination of a *general rule or norm in the abstract.* However, as the original panel found, an examination of the "*effects*" of the general statutory and regulatory provisions establishing a subsidy program "*cannot be conducted in the abstract*" because they must be considered in light of the market-based effects of the measures.[90] Thus, Brazil considers that serious prejudice claims are among those that cannot be readily classifiable as "as such" and "as applied."

b) How these claims differ from claims against programs as applied?

115. As explained below, there is no practical difference in terms of this compliance Panel's ultimate finding that the United States has not complied with Article 7.8 of the *SCM Agreement.*

116. While Brazil's request for the establishment of a panel does not make an explicit "as applied" claim, that request is broad enough to encompass a claim described in these terms, if this compliance Panel were to deem it necessary to affix an "as applied" label to it. As noted above, Brazil's claims challenge, *inter alia*, the marketing loan and counter-cyclical subsidies, to the extent they cause adverse effects. Brazil sets out evidence and argument addressing the effects of the subsidy programs, including reference to the operation (or application) of the programs in the prior periods. If the compliance Panel finds that the marketing loan and counter-cyclical subsidies cause present serious prejudice, then the compliance Panel would find that the United States has not taken appropriate steps to withdraw the subsidies or to remove their adverse effects.

[89] Appellate Body Report, *EC – Selected Customs Matters*, para. 165.
[90] Panel Report, *U.S. – Upland Cotton*, para. 7.1198.

117. If the compliance Panel were to label Brazil's claims as "as applied" adverse effects claims, then presumably those claims would be cast in terms of whether the application of the marketing loan and counter-cyclical payment "programs" cause serious prejudice. Assuming the compliance Panel were to find that the application of the marketing loan and counter-cyclical "programs" (presumably accomplished through the means of mandatory and price-contingent "payments") causes serious prejudice, the compliance Panel would find that the United States had failed, pursuant to Article 7.8 of the *SCM Agreement*, to take appropriate steps to withdraw the marketing loan and counter-cyclical program subsidies or to remove their adverse effects.

118. Brazil again expresses its agreement with the United States' observation in *EC – Selected Customs Matters* that certain claims under the covered agreements are "not readily classifiable in the categories of 'as such' and 'as applied.'"[91]

13. In paragraph 45 of its Rebuttal Submission, Brazil refers to the failure of the United States "to implement the original recommendation of the DSB requiring the United States to take actions concerning its present statutory and regulatory framework providing for marketing loan and counter-cyclical payments".

a) Does Brazil consider that the statement in paragraph 7.1501 of the original panel report that "the United States is obliged to take action concerning its present statutory and regulatory framework..." forms an integral part of the recommendation made by the original panel in paragraph 8.3(d) of its report?

119. Yes, Brazil considers that the statement in paragraph 7.1501 of the original panel report forms an integral part of the recommendation made by the original panel in paragraph 8.3(d) of its report. The statement in paragraph 7.1501 is part of the assessment of the matter undertaken by the original panel and is found in the portion of the original panel report dealing with "findings." In paragraph 8.1, the original panel stated that, "[i]n light of the findings above, we conclude as follows …." The original panel then listed its conclusions, including its conclusions regarding present serious prejudice. In paragraph 8.3, the original panel sets forth its recommendations "[i]n light of these conclusions." This demonstrates that also the original panel considered its findings – including its statement in paragraph 7.1501 – to form an integral part of, and basis for, its conclusions and recommendations. As noted, these findings were never appealed by the United States.

b) Does Brazil consider that the absence of actions by the United States "concerning its present statutory and regulatory framework providing for marketing loan and counter-cyclical payments" is in itself a sufficient basis for this Panel to find that the United States has not complied with the DSB recommendation under Article 7.8 of the SCM Agreement?

120. Yes, Brazil considers that the absence of actions by the United States "concerning its present statutory and regulatory framework providing for marketing loan and counter-cyclical payments" is in itself a sufficient basis for the compliance Panel to find that the United States has not complied with the DSB recommendation under Article 7.8 of the *SCM Agreement*.

121. However, Brazil also demonstrates that the marketing loan and counter-cyclical payments programs, as well as payments mandated thereunder, cause adverse effects in violation of Article 5(c) and 6.3 of the *SCM Agreement*. In other words, following the U.S. repeal of the Step 2 subsidy, the new basket of measures involving these two subsidies causes significant price suppression in the world market for upland cotton and an increase in the U.S. world market share, in violation of Articles 5(c) and 6.3(c) and (d). In establishing these violations, Brazil provides evidence on the structure, design and operation of the subsidy programs, including the nature and magnitude of the

[91] Appellate Body Report, *EC – Selected Customs Matters*, para. 165.

payments mandated by them, as well as the relevant conditions of competition in the world market for upland cotton.[92]

122. Should the compliance Panel find that the absence of actions by the United States is a sufficient basis to conclude that the United States has not complied with the DSB recommendation under Article 7.8 of the *SCM Agreement*, Brazil nevertheless requests that the compliance Panel make factual findings that these subsidies continue to cause significant price suppression and an increase in the U.S. world market share, in the event that these factual findings prove to be relevant for an appeal.

c) Is there any difference, in Brazil's view, between, on the one hand, the nature of the action the United States was obliged to take with respect to its statutory and regulatory framework as a consequence of the recommendation in paragraph 8.3(d) of the original panel report and, on the other, the nature of the action the United States would have been obliged to take if the original panel had found that the relevant provisions of this statutory and regulatory framework were WTO-inconsistent as such?

123. No, the action required by the United States would have been the same in both cases.

124. The scope of the United States' implementation obligations turns on the identity of the measures that the original panel found to be WTO-inconsistent. In this dispute, as explained in reply to Question 11, the entirety of the original panel's findings demonstrate that the measures found to be WTO-inconsistent included the "statutory and regulatory framework" establishing the contested subsidy programs. As a result, the United States' implementation obligations required it to take action to amend or repeal this statutory and regulatory framework.

125. The original panel expressly stated that the *contested measures* included "*current legislative and regulatory provisions* providing for the payment" of the contested subsidies, as well as payments mandated by the programs throughout the panel proceedings.[93] Consistent with this statement, the original panel's examination of the contested measures "focus[ed]" on the *design, structure and operation* of the contested *programs*, as set forth in the statutory and regulatory framework establishing the programs.[94] In contrast, the original panel found that it was not necessary to quantify precisely the level of payments made under the contested programs.[95] Instead, as part of a "quantitative" assessment of the programs, it considered, "to some extent", the "general order of magnitude" of the payments made under the programs.[96]

126. In keeping with the description of the contested measures, and the examination of those measures, the original panel held, in paragraph 7.1501, that the measures causing "adverse effects" included the "*statutory and regulatory framework*" establishing the contested subsidy *programs*.

127. Immediately after making this statement, in paragraph 7.1503, the original panel also emphasized that, during implementation, the United States was required to "*significantly transform[]*" the contested subsidy programs such that, after implementation, any subsidy programs maintained by the United States would be "*manifestly different*" from those originally contested. For this reason, the original panel found that there was no need to examine whether the contested programs threatened serious prejudice during "the remaining period of application of the FSRI Act of 2002", that is

[92] Brazil's First Written Submission, Sections 7-9; Brazil's Rebuttal Submission, Sections 2.3-2.4. In its Opening Statement at today's meeting with the compliance Panel, Brazil will present further rebuttal evidence.

[93] Panel Report, *U.S. – Upland Cotton*, paras. 7.187 and 7.337.

[94] Panel Report, *U.S. – Upland Cotton*, para. 7.1194.

[95] Panel Report, *U.S. – Upland Cotton*, paras. 7.1173 and 7.1194.

[96] Panel Report, *U.S. – Upland Cotton*, paras. 7.1173 and 7.1194.

through MY 2007.[97] In short, the United States was required to make future payments under "manifestly different" "statutory and regulatory framework", or not make them at all. Nor was it necessary, for the same reasons, to rule on the WTO-inconsistency of the subsidy programs "as such".[98]

128. The findings or the original panel, in paragraphs 7.1501 and 7.1503 of its report, demonstrate that the measures found to be WTO-inconsistent included the "*statutory and regulatory framework*" establishing the contested subsidy *programs*.

129. This is also confirmed by paragraph 8.1(g)(i) of the original panel report, in which the Panel concludes that "*mandatory price-contingent* United States subsidy *measures*" are inconsistent with Article 5(c) and 6.3(c) of the *SCM Agreement*. As noted in reply to Question 11, the measures referenced in this paragraph are the subsidy programs, including mandatory payments, and not the "payments" on their own, because "payments" alone do not mandate anything.

130. The action required by the United States to "significantly transform" – or withdraw – the "*statutory and regulatory framework*" establishing the contested subsidy programs is the same as the action that the United States would have been obliged to take if the measures had been found to be "as such" WTO-inconsistent.

14. Could Brazil please explain how this Panel should interpret the relationship between the three categories of measures identified in paragraph 3.1(v),(vii) and (viii) of the original panel report? Is it the view of Brazil that "subsidies provided" or "subsidies mandated to be provided" must be interpreted to encompass both payments of subsidies and the regulatory provisions pursuant to which such payments were "provided" or "mandated to be provided"?

131. The compliance Panel's question refers to three categories of measure identified in paragraphs 3.1***(v)***, (vii) and (viii). Brazil believes that the Panel's question is intended to refer to paragraphs 3.1***(vi)***, (vii) and (viii), and answers on that basis.

132. The measures identified in paragraphs 3.1(vi) and 3.1(vii) must be interpreted to encompass the statutory and legislative framework establishing the contested subsidy programs, as well as payments mandated by those programs. Under paragraph 3.1(viii), the measures encompass simply the statutory and legislative framework establishing the contested programs. Brazil notes that its goal in defining these different categories of measures was to be *over-inclusive* in identifying comprehensively the range and combination of measures included in the original panel's terms of reference.

133. As explained in answers to Questions 11 and 13(c), the original panel found "present" serious prejudice with respect to the measures in paragraph 3.1(vi), that is the statutory and regulatory framework establishing the contested subsidy programs, as well as payments mandated by those programs. As the original panel stated in paragraphs 7.1501 and 7.1503 of its report, the United States' implementation obligations required it, therefore, to take action with respect to that framework to staunch the flow of the mandated payments.

15. Does Brazil agree or disagree with the United States that the listing of certain legislative and regulatory provisions in paragraph 7.1107 of the original panel report reflects the original panel's view that "payments under a program constitute programs 'as applied' "? [Paragraphs 46-47 of the Rebuttal Submission of the United States]

[97] Panel Report, *U.S. – Upland Cotton*, para. 7.1500.
[98] Panel Report, *U.S. – Upland Cotton*, para. 7.1511.

134. Brazil does not agree with the United States that the listing of certain legislative and regulatory provisions in paragraph 7.1107 of the original panel report reflects the original panel's view that "payments under a program constitute programs 'as applied.'" In fact, the original panel report indicated that the original panel did not make "as applied" findings (either expressly or by implication).

135. The United States attempts to rewrite the original panel report such that its implementation obligation would be limited to removing adverse effects of Step 2, marketing loan, and counter-cyclical payment subsidies for MY 1999-MY 2002. Brazil has set forth in detail its position regarding the original panel's findings in its Response to U.S. Requests for Preliminary Rulings. It reiterates those arguments together with its answers to the compliance Panel's earlier questions, in particular question 11, above. Brazil sets out additional explanation for its views below.

136. The United States' "as applied" argument incorrectly transforms the original panel's decision to use MY 2002, and the longer period of MY 1999-MY 2002, as "reference periods", into a period that circumscribes the *measures* involved in Brazil's present serious prejudice claims. Yet, as explained in reply to Question 11, the "reference period"[99] was merely a methodological tool used to marshal evidence and assess data. Nothing suggests that the original panel intended to restrict its conclusions and recommendations to any historical period of "effects".

137. Had the original panel intended to limit the measures at issue, as a jurisdictional matter, to payments in a particular historical period, any such finding would have contradicted its ruling that its terms of reference included mandatory payments made throughout the original panel proceedings.[100] Also, if the original panel's present serious prejudice findings were limited to payments made in MY 2002, or any other historical period, this would contradict its conclusion, in paragraph 7.1501 of its report, that changes to statutory framework resulting from its *present* serious prejudice obviated the need for examination of a *threat* of serious prejudice through MY 2007.

138. Moreover, the original panel's serious prejudice conclusion, set out in paragraph 8.1(g)(i) of its report, did not reference *any* time period. The original panel concluded that:

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

139. The United States claims that this conclusion is limited to the effects caused by mandatory price-contingent United States subsidy payments made only *during MY 2002*, or effects caused by mandatory price-contingent subsidy payments made only *during* MY 1999-2002. However, if applicable, any such temporal limitation would have been set out expressly in both the description of the measures at issue in paragraph 7.1107, and the panel's conclusion in paragraph 8.1(g)(i). Yet, as a jurisdictional matter, there is no temporal limitation on the measures at issue in these or any other paragraph of the original panel report.

140. Further, the final panel report was issued to the parties on 18 June 2004 – 10 ½ months *after* MY 2002 ended and only six weeks *before* MY 2003 ended. By the time the Dispute Settlement Body adopted the "present" serious prejudice findings, conclusions and recommendations on

[99] Panel Report, *U.S. – Upland Cotton*, para. 7.1195 (heading title for Section VII.G.3(e)).
[100] Panel Report, *U.S. – Upland Cotton*, para. 7.187.

21 March 2005, almost two-thirds of MY 2004 had been completed. If the intention of the original panel had been to make an "as applied" finding limited to serious prejudice caused *only* in MY 2002 or *only* in MY 1999-2002, it would have used the *past* tense in its conclusions in paragraph 8.1(g)(i) of its report. Instead, it used the *present* tense: "the effect of mandatory price-contingent United States subsidy measures … *is* significant price suppression …."). That conclusion and the accompanying recommendation in paragraph 8.3 – along with the U.S. obligation under Article 7.8 to take appropriate steps to remove the adverse effects or withdraw the subsidy – continues to be applicable today.

141. Significantly, the original panel's findings that the United States was obligated to take action concerning its "present statutory and regulatory framework" existing in MY 2003 as a result of the panel's "present" serious prejudice findings also is inconsistent with the U.S. argument that the original panel made an "as applied" finding. The original panel found that "it is clear that the existing subsidy programs are currently envisaged to remain in effect between MY 2003-MY 2007." And immediately after making this finding, the original panel held:

> Because the Panel's "present" serious prejudice findings include findings of inconsistency that deal with the FSRI Act of 2002 and subsidies granted thereunder in MY 2002, the United States is obligated to take action concerning its present statutory and regulatory framework as a result of our "present" serious prejudice findings. We recall that, pursuant to Article 7.8 of the *SCM Agreement*, the United States is under an obligation to "take appropriate steps to remove the adverse effects or … withdraw the subsidy.[101]

142. If the original panel had made an "as applied" finding limited to only *past* effects of *past* mandatory and price-contingent payments, then there would be no reason for the original panel to state in June of 2004 that "*the United States is obligated to take action concerning its present statutory and regulatory framework as a result of our "present" serious prejudice findings*." Moreover, there would also have been every reason for the original panel to examine a threat of serious prejudice through MY 2007.

143. Instead, under the U.S. theory, because the original panel made only "as applied" findings of present serious prejudice for past payments, and because it neglected to make any "threat" findings, the United States had every right to continue making massive *future* mandatory and price-contingent payments during MY 2003, MY 2004, and MY 2005. On this view, when the United States was required to "take appropriate steps" in *MY 2005* to withdraw the adverse effects of payments made in MY 1999-MY 2002, the United States could credibly assert that the $5.4 billion paid out in marketing loan counter-cyclical subsidies in MY 2003-2005[102] were not subject to any implementation obligations, and were *the* intervening cause of significant price suppression in MY 2005.

144. In conclusion, the original panel *never* described its findings, conclusions or recommendations as being "as applied." Nor did the original panel conclude that Brazil's present serious prejudice claims constituted only "as applied" claims limited to payments made within a specified period. As demonstrated above, neither the panel's terms of reference, the measures the original panel found to be applicable to Brazil's serious prejudice claims in paragraph 7.1107 of its report, or the measures the original panel concluded cause significant price suppression were so limited.

145. Finally, even assuming that the original panel's findings of present serious prejudice were "as applied" findings limited to marketing loan and counter-cyclical payments made during a particular

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[101] Panel Report, *U.S. – Upland Cotton*, para. 7.1501.
[102] Exhibit Bra-471 (Table 6 in Detail).

historical period (*quod non*), subsequent payments made under the same program are also subject to the United States' implementation obligations.

146. In *U.S. – Softwood Lumber IV (21.5)*, Canada challenged a periodic review measure that was not declared by the United States to be a "measure taken to comply". The effect of the periodic review was to render nugatory the declared measure taken to comply. Following findings in *Australia – Leather (21.5)* and *EC – Bed Linen (21.5)*, the Appellate Body upheld the compliance panel's finding that the review measure was a WTO-inconsistent "measure taken to comply":

> Some measures with a particularly close relationship to the declared "measure taken to comply", and *to the recommendations and rulings of the DSB*, may also be susceptible to review by a panel acting under Article 21.5.[103]

147. In this dispute, subsequent payments made by the United States pursuant to the marketing loan and counter-cyclical payment programs have such a close relationship to measures subject to the original proceedings, and to the DSB's recommendations and rulings, that they are susceptible to review by this compliance Panel. In particular, the payments collectively constitute an unbroken stream of identical subsidies. The payments subject to the DSB's recommendations and the payments subject to these proceedings are mandated by the very same subsidy programs; they are made to the very same recipients; they support the very same crops; and they are granted on the very same terms and conditions. The subsequent payments are, therefore, "clearly connected" and "inextricably linked" to the measures found to be WTO-inconsistent in the original proceedings.[104]

148. Indeed, the connection between the payments is much closer than the connection between the measures at issue in *U.S. – Softwood Lumber IV (21.5)*, *Australia – Leather (21.5)* and *EC – Bed Linen (21.5)*. In sum, Brazil's dispute with the United States in these proceedings regarding the adverse effects of marketing loan and counter-cyclical subsidies is identical to its dispute regarding precisely the same subsidies in the original proceedings. The only significant change is that the level of the subsidies has *increased* with time.

149. Similar to the U.S. arguments in *U.S. – Softwood Lumber IV (21.5)*, if the U.S. view that subsequent marketing loan and counter-cyclical payments are *not* subject to this compliance Panel's review, the U.S. grant of recurring subsidies become "*a moving target that escape from [the WTO subsidy] disciplines*".[105] Subsequent mandatory payments would always have to be subject to new dispute settlement proceedings, and by the time these proceedings were completed, the effects of the latest payments would be superseded by yet more payments, which could in turn only be challenged in yet another original panel process. WTO dispute would dissolve into a "Groundhog Day" situation, with no remedy available to Members suffering adverse effects.[106]

150. Thus, even if the United States were correct (*quod non*), that the DSB's recommendations pertain solely to marketing loan and counter-cyclical payments made during a defined historical period, Brazil is entitled to challenge subsequent marketing loan and counter-cyclical payments in these compliance proceedings because these payments are "inextricably linked".

16. Could Brazil clarify whether or not its claim in this Article 21.5 proceeding regarding a threat of serious prejudice caused by marketing loan and counter-cyclical payments is a claim with respect to the marketing loan and counter-cyclical payment programs as such? [Paragraphs 237-314 of the First Written Submission of Brazil]

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[103] Appellate Body Report, *U.S. – Softwood Lumber IV (21.5)*, para. 77.
[104] Appellate Body Report, *U.S. – Softwood Lumber IV (21.5)*, para. 79.
[105] Panel Report, *U.S. – Softwood Lumber IV (Article 21.5 – Canada)*, para. 4.30.
[106] Panel Report, *U.S. – Softwood Lumber IV (Article 21.5 – Canada)*, para. 4.30, *quoting* arguments of the European Communities.

151. The scope of the compliance Panel's terms of reference in these proceedings is determined by the Brazil's Request for the Establishment of a Panel.[107] Paragraph 20 of the Panel Request specifies:

> Specifically, Brazil believes that the US marketing loan and counter-cyclical payment programs under the FSRI Act of 2002, as amended, *as well as payments mandated to be made thereunder*, threaten to cause significant price suppression in the world market for upland cotton in marketing years 2006 and until the expiry or repeal of these programs.[108]

Thus, Brazil claims that the contested subsidy programs, as well as payments to be made under those programs, threaten to cause serious prejudice.

152. To examine this claim, following the approach of the original panel, as upheld by the Appellate Body, the compliance Panel must consider the *structure, design and operation* of the contested *programs*, as set forth in the statutory and regulatory framework establishing the programs.[109] In addition, along with other evidence, the compliance Panel may also consider the general order of the magnitude of payments made under the contested programs in the past. On this basis, the compliance Panel may establish whether the effect of the contested programs is to threaten serious prejudice in the future.[110]

153. Brazil recalls its agreement with the United States' observation in *EC – Selected Customs Matters* that certain claims under the covered agreements are "not readily classifiable in the categories of 'as such' and 'as applied.'"[111] Brazil considers that serious prejudice claims are among those that cannot be readily classifiable as "as such" and "as applied."

Questions to the United States

17. The United States argues in paragraph 16 of its Rebuttal Submission that "[a]ccording to Brazil, its claims apply not only to the marketing loan and counter-cyclical payment programs, as such, but to the programs in addition to all payments authorized under the programs" (original emphasis). The United States also argues in this respect that "it is abundantly clear that the original panel did not make any finding under Article 5(c) and 6.3(c) of the SCM Agreement against the marketing loan and counter-cyclical payment programs, as such, whether alone or in addition to payments". [Paragraph 43 of Rebuttal Submission of the United States]

a) How does the United States respond to the argument of Brazil that the United States mischaracterizes Brazil's claims in these proceedings in that Brazil is not challenging the subsidy programs at issue as such? [Paragraph 31 of Submission of Brazil to the Panel Regarding US Requests for Preliminary Ruling; paragraph 33 of Rebuttal Submission of Brazil]

b) Could the United States also comment in this regard on the arguments in paragraph 31 of the Third Party Submission of Chad? Does the United States agree or disagree with the proposition that statutory or regulatory provisions can be challenged on an as applied basis and that Brazil's claims in the original proceeding "were as applied claims regarding measures that included legislative and regulatory provisions"?

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[107] WT/DS267/30.
[108] WT/DS267/30 (footnote omitted).
[109] Panel Report, *U.S. – Upland Cotton*, para. 7.1194.
[110] Panel Report, *U.S. – Upland Cotton*, paras. 7.1173 and 7.1194.
[111] Appellate Body Report, *EC – Selected Customs Matters*, para. 165.

18. The United States submits that the only measures subject to the DSB's recommendation under Article 7.8 of the SCM Agreement are payments made under the Step 2, marketing loan, and counter-cyclical payment programs in 1999-2002. The United States also asserts, in this regard, that Brazil fails to submit evidence "as to the present effects, if any, of the measures that were subject to the original panel's actionable subsidy finding".

a) Do these statements mean that the United States considers that the DSB recommendation under Article 7.8 of the SCM Agreement only obliged the United States to ensure that payments made in 1999-2002 would no longer have any adverse effects?

b) Could the United States comment on the argument of New Zealand in paragraph 4.08 of the Third Party Submission of New Zealand?

19. Regarding the argument of the United States that the marketing loan and counter-cyclical payments programs are not measures "taken to comply", is it the view of the United States that Article 21.5 of the DSU only applies to measures actually taken by a party to comply and does not apply to measures that a Member should have taken to comply?

20. How does the United States respond to the argument in the Third Party Submission of Japan that the Appellate Body report in EC – Bed Linen (Article 21.5 – India) does not support the argument of the United States that the marketing loan and counter-cyclical payments programs are not within the scope of this Article 21.5 proceeding?

3. Claim of Brazil regarding the failure of the United States to comply with the DSB recommendations between 21 September 2005 and 1 August 2006

Questions to Brazil

21. Could Brazil please explain whether its request for a finding that the United States failed to comply with the DSB recommendations between 21 September 2005 and 1 August 2006 is supported by prior panel practice in Article 21.5 proceedings? [Paragraph 68 of the Rebuttal Submission of the United States]

154. In *Australia – Salmon(21.5)*, Canada made claims similar to those advanced by Brazil in this dispute on the non-existence of compliance measure during a specified period following the end of the implementation period. In that dispute, Australia adopted certain compliance measures after the expiry of the reasonable period of time on 6 July 1999. Canada claimed that, during the period between 6 July 1999 and the adoption of the compliance measures, no compliance measures existed. The compliance panel found as follows:

> [T]he date of entry into force of the new measures varies according to the products covered. In all cases, the entry into force – and thus the "existence" of the measures taken to comply – occurred *subsequent* to 6 July 1999, the date of expiry of the reasonable period of time given to Australia to implement the DSB recommendations and rulings. Since, in this case, Australia was under an obligation to implement the DSB recommendations and rulings by the end of the reasonable period of time,[154] we find that for the period of time that the new measures did not and will not apply subsequent to 6 July 1999, no measures taken to comply existed or will exist in the sense of Article 21.5.

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[154] Since Australia and Canada could so far not agree on compensation as a temporary measure pursuant to Article 22.1 of the DSU, Australia was under an obligation to comply

> with DSB recommendations and rulings by the end of the reasonable period of time. If it did not do so, Australia could face suspension of concessions or other obligations under Article 22.6 of the DSU.[112]

155. The findings of the compliance panel in *Australia – Salmon (21.5)*, therefore, support fully Brazil's claims.

156. Brazil notes that, in this dispute, there are two arbitrations pending under Article 22.6 of the DSU and Articles 4.11 and 7.10 of the *SCM Agreement* respectively. Thus, similarly to the situation in *Australia – Salmon 21.5*, the United States could face countermeasures or suspension of concessions or other obligations under those provisions with respect to non-implementation by the end of the implementation period.

157. Finally, Brazil notes that no such arbitration was pending in the two cases cited by the United States: *EC – Bed Linen (21.5)* and *U.S. – Shrimp (21.5)*.

22. How does Brazil respond to the argument of the European Communities that "the lack of positive action taken by the United States to comply with the panel and Appellate Body's findings and recommendations between the implementation date of 21 September 2005 and 31 July 2006 is not necessarily fatal to its defence"? [Paragraph 48 of the Third Party Submission of the European Communities]

158. Brazil disagrees that a subsidizing Member implementing pursuant to Article 7.8 of the *SCM Agreement* can do nothing and be in compliance with the findings, conclusions, and recommendations of panels and the Appellate Body. By 21 September 2005, the United States was required to take affirmative action under Article 7.8 of the *SCM Agreement.* But it did nothing.

159. Article 7.8 requires action, not inaction, no later than the end of the six-month implementation period following adoption by the DSB of the panel or Appellate Body report contemplated by Article 7.9 of the *SCM Agreement.* Read together, these two Articles impose an obligation that a subsidizing Member "shall take appropriate steps to remove the adverse effects or shall withdraw the subsidy" during that six-month period.

160. During this period, a Member may choose to withdraw the subsidy. That involves some type of statutory, regulatory, or executive action to eliminate a subsidy.

161. The second part of Article 7.8 provides that a Member "shall *take* appropriate *steps* to remove the adverse effects." The ordinary meaning of the term "take" is "to undertake and perform (a specified function, service, etc.)" or "to perform, make, or do (an act, movement, etc.)".[113] In turn, the ordinary meaning of "step" is "the action, measure, or proceeding, especially one of a series, which leads towards a result."[114] Thus, to "take" appropriate "steps" means to *undertake action* that fully removes the adverse effects to the interests of another Member. What constitutes the specific "appropriate" steps to be taken will vary according to the particular facts in a given situation. Nonetheless, taking steps, or undertaking some affirmative action, to remove the adverse effects of "any subsidy" is required by this part of Article 7.8. Doing nothing is not undertaking action.

162. Having taken *no* action whatsoever by 21 September 2005, the United States had "not taken appropriate steps to remove the adverse effects of the subsidy or withdraw the subsidy within six months from the date when the DSB adopts the panel report and the Appellate Body report".

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[112] Panel Report, *Australia – Salmon (Article 21.5 – Canada)*, para. 7.30. *See, also*, para. 8.1(i) of the Panel's findings and conclusions. Underlining added.

[113] New Shorter Oxford English Dictionary, 1993 Edition, Vol. 2, pp. 3207, 3208.

[114] New Shorter Oxford English Dictionary, 1993 Edition, Vol. 2, p. 3050.

163. In its responses to questions 24 and 25, due to the Panel on 6 March, Brazil will explore further the proper interpretation of Article 7.8, alone and in conjunction with Article 21.5 of the DSU. Those responses will bear on the matter covered by the Panel in question 22.

Question to the United States

23. Does the United States consider that the text of Article 21.5 of the DSU should be interpreted to mean that a compliance panel may only review the "existence" or "consistency" with a covered agreement of measures taken to comply as of the date that the matter was referred to the panel and not as of the date of the end of the implementation period? [Paragraph 68 of the Rebuttal Submission of the United States]

ANNEX D-7

RESPONSES OF BRAZIL TO THE PANEL'S FIRST SET OF QUESTIONS (SECTIONS D&E)

(6 March 2007)

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Brazil – Aircraft (21.5)	Appellate Body Report, *Brazil – Export Financing Program for Aircraft – Recourse by Canada to Article 21.5 of the DSU*, WT/DS46/AB/RW, adopted 4 August 2000, DSR 2000:VIII, 4067.
Brazil – Aircraft (21.5)	Panel Report, *Brazil – Export Financing Program for Aircraft – Recourse by Canada to Article 21.5 of the DSU*, WT/DS46/RW, adopted 4 August 2000, modified by Appellate Body Report, WT/DS46/AB/RW, DSR 2000:IX, 4093.
Brazil – Aircraft (21.5 II)	Panel Report, *Brazil – Export Financing Program for Aircraft – Second Recourse by Canada to Article 21.5 of the DSU*, WT/DS46/RW/2, adopted 23 August 2001, DSR 2001:X, 5481.
Canada – Aircraft	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft*, WT/DS70/AB/R, adopted 20 August 1999, DSR 1999:III, 1377.
Canada – Aircraft (21.5)	Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft – Recourse by Brazil to Article 21.5 of the DSU*, WT/DS70/AB/RW, adopted 4 August 2000, DSR 2000:IX, 4299.
Canada – Aircraft Credits and Guarantees	Panel Report, *Canada – Export Credits and Loan Guarantees for Regional Aircraft*, WT/DS222/R and Corr.1, adopted 19 February 2002, DSR 2002:III, 849.
U.S. – FSC (21.5)	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW, adopted 29 January 2002, DSR 2002:I, 55.
U.S. – FSC (21.5 II)	Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Second Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW2, adopted 14 March 2006.
U.S. – Shrimp (21.5)	Appellate Body Report, *United States – Import Prohibition of Certain Shrimp and Shrimp Products – Recourse to Article 21.5 of the DSU by Malaysia*, WT/DS58/AB/RW, adopted 21 November 2001, DSR 2001:XIII, 6481.
U.S. – Softwood Lumber IV	Appellate Body Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R, adopted 17 February 2004, DSR 2004:II, 571.
U.S. – Softwood Lumber IV (21.5)	Appellate Body Report, *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada – Recourse by Canada to Article 21.5 of the DSU*, WT/DS257/AB/RW, adopted 20 December 2005.
U.S. – Softwood Lumber VI (21.5)	Appellate Body Report, *United States – Investigation of the International Trade Commission in Softwood Lumber from Canada – Recourse to Article 21.5 of the DSU by Canada*, WT/DS277/AB/RW, adopted 9 May 2006.
U.S. – Upland Cotton	Panel Report, *United States – Subsidies on Upland Cotton*, WT/DS267/R, and Corr.1, adopted 21 March 2005, modified by Appellate Body Report, WT/DS/267/AB/R.

D. CLAIMS OF BRAZIL REGARDING PRESENT SERIOUS PREJUDICE

1. General

Questions to both parties

24. Could the parties explain how they interpret the phrases "take appropriate steps to remove the adverse effects" and "withdraw the subsidy" in Article 7.8 of the SCM Agreement?

1. The phrases "take appropriate steps to remove the adverse effects" and "withdraw the subsidy" in Article 7.8 of the *SCM Agreement* require action that secures the full and complete removal of any adverse effects, or the full withdrawal of any actionable subsidy found to cause adverse effects.

2. As Brazil stated in its answer to Question 22, the terms used in Article 7.8 require *action* by a defending Member, rather than *inaction*, and that removal of the adverse effects or withdrawal of the subsidy must be *complete*, rather than *partial*.

3. Before addressing this interpretive question, Brazil notes a threshold question that must be addressed by a compliance Panel confronted with recommendations under Article 7.8 of the *SCM Agreement* – what is the "subsidy" to be withdrawn, or the adverse effects of which must be removed in the present dispute?

4. In its 26 February response to question 11, Brazil explained that the subsidy subject to the Article 7.8 recommendation includes both the legislative and regulatory subsidy programs in the FSRI Act of 2002 and the price-contingent and mandatory payments made under those programs. In its 26 February response to question 15, Brazil explained that even if the original panel's findings of present serious prejudice were limited to marketing loan and counter-cyclical payments ("CCP") made during a particular historical period (*quod non*), subsequent payments made under the same program are also subject to the United States' implementation obligations. [1]

5. Article 7.8 has two implementation elements set out in the phrases "take appropriate steps to remove the adverse effects" and "withdraw the subsidy", and demonstrates that action, rather than inaction, is required of an implementing Member.

6. The ordinary meaning of the term "take" is "to undertake and perform (a specified function, service, etc.)" or "to perform, make, or do (an act, movement, etc.)".[2] In turn, the ordinary meaning of "step" is "the action, measure, or proceeding, especially one of a series, which leads towards a result."[3] Because the object of the action is "adverse effects", the "appropriate" "steps" must involve action that removes the adverse effects to the interests of another Member.

7. What constitutes the specific "appropriate" steps to take to remove the adverse effects will vary according to the facts of each case. Fundamentally, steps can only be "appropriate" if they achieve full and permanent removal of the adverse effects. For example, the original panel identified the particular *appropriate step* under Article 7.8 that the United States must take regarding the "basket" of price-contingent and mandatory subsidies found to cause present significant price suppression:

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[1] Appellate Body Report, *U.S. – Softwood Lumber IV (21.5)*, para. 77 ("Some measures with a particularly close relationship to the declared 'measure taken to comply', and *to the recommendations and rulings of the DSB*, may also be susceptible to review by a panel acting under Article 21.5.").

[2] New Shorter Oxford English Dictionary, 1993 Edition, Vol. 2, pp. 3207, 3208.

[3] New Shorter Oxford English Dictionary, 1993 Edition, Vol. 2, p. 3050.

> [b]ecause the Panel's "present'" serious prejudice findings include findings of inconsistency that deal with the FSRI Act of 2002 and subsidies granted hereunder in MY 2002, *the United States is obliged to take action concerning its present statutory and regulatory framework as a result of our "present" serious prejudice findings. We recall that, pursuant to Article 7.8 of the SCM Agreement, the United States is under an obligation to "take appropriate steps to remove the adverse effects or … withdraw the subsidy*.[4]

8. At no time did the original panel suggest that an "appropriate step" to remove the adverse effects could involve doing nothing other than waiting for the effects of past payments to dissipate. As Article 7.8 requires action, rather than inaction, to do so would have rendered both Articles 6.3 and 7.8 of the *SCM Agreement* inutile. Any objective reading of the original panel's findings demonstrates that it expected the United States to take action to ensure that present serious prejudice would not continue during the remaining life of the FSRI Act of 2002.[5]

9. The second relevant phrase found in Article 7.8 is "withdraw the subsidy." The structure and placement of the phrase "take appropriate steps," as confirmed by both the French and Spanish versions of the official texts,[6] indicates that it only qualifies and refers to the phrase "remove the adverse effects" – not "withdraw the subsidy."

10. In examining the meaning of the identical phrase "withdraw the subsidy" in Article 4.7 of the *SCM Agreement*, the Appellate Body, in *Brazil – Aircraft (21.5)*, required affirmative action by the defending Member:

> Turning to the ordinary meaning of "withdraw", we observe first that this word has been defined as "remove" or "take away", and as "to take away what has been enjoyed; to take from." This definition suggests that "withdrawal" of a subsidy, under Article 4.7 of the *SCM Agreement*, refers to the "removal" or "taking away" of that subsidy.[7]

11. Given the identity of this aspect of Articles 4.7 and 7.8, the Appellate Body's finding regarding the meaning and action required to "withdraw the subsidy" in Article 4.7 applies also to Article 7.8.

12. A subsidy could be "removed" or "taken away" by the implementing Member enacting new legislation or taking regulatory steps to cease operation or disbursements of payments under the terms of the subsidy measure. As demonstrated above, Article 7.8 requires *affirmative action* to remove the adverse effects or withdraw the subsidy. Inaction is not sufficient.

13. Moreover, *full* removal of the adverse effects or *full* withdrawal of the subsidy is also required. As noted by the Appellate Body, "full withdrawal of a prohibited subsidy within the meaning of Article 4.7 of the *SCM Agreement* cannot be achieved by a 'measure taken to comply' that replaces the original subsidy with yet another subsidy found to be prohibited."[8] The same reasoning should apply to Article 7.8. Removing the adverse effects of a subsidy measure or withdrawing a

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[4] Panel Report, *U.S. – Upland Cotton*, para. 7.1501.

[5] Panel Report, *U.S. – Upland Cotton*, paras. 7.1499-7.1503, 8.1(g)(i).

[6] The Spanish text states: "… el Miembro que otorgue o mantenga esa subvención adoptará las medidas apropiadas para eliminar los efectos desfavorables o retirará la subvención." The French text states: "... le Membre qui accorde ou maintient cette subvention prendra des mesures appropriées pour eliminer les effets défavorables ou retirera la subvention."

[7] Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 45 (footnotes omitted).

[8] Appellate Body Report, *U.S. – FSC (21.5 II)*, para. 83.

subsidy measure found to cause adverse effects, and subsequently *replacing* it with another subsidy measure that causes adverse effects, is not sufficient.

14. Even assuming, *arguendo*, that the only finding by the original panel was with respect to adverse effects flowing from MY 1999-2002 payments, it is insufficient for the United States to satisfy its obligation to remove the adverse effects or withdraw the subsidy by simply allowing the effects of MY 1999-2002 payments to wane and die a natural death, only to be replaced by even higher price-contingent and mandatory payments during the period MY 2003-2005. Brazil has demonstrated that these "replacement" payments cause similar, if not even greater, significant price suppression in the world market for upland cotton.

25. How do the parties interpret the relationship between Article 7.8 of the SCM Agreement and Article 21.5 of the DSU?

15. Brazil refers the Panel to its answer to Question 24, above, which sets forth the particular characteristics of Article 7.8 of the *SCM Agreement.*

16. Article 7.8 of the *SCM Agreement* is a special and *additional* rule, under Appendix 2 of the DSU. Because there is no conflict between Article 7.8 and Article 21.5 of the DSU, Article 7.8 does not *replace* Article 21.5 in compliance proceedings, but instead *supplements* Article 21.5.

17. An Article 21.5 compliance panel assessing implementation under Article 7.8 plays two, overlapping roles. First, the compliance panel assesses whether an implementing Member has taken affirmative action constituting either appropriate steps to remove the adverse effects, or withdrawal of the subsidy causing those adverse effects. Second, the compliance panel assesses whether any measures taken to comply exist, and if they exist, whether those measures, in their totality[9], are consistent with the covered agreements.

18. As a practical matter, these two assessments can overlap, and may involve the same evidence. But there may be instances in which a Member has, *e.g.*, "withdrawn the subsidy" under Article 7.8 but, nevertheless, *is not* in compliance with Articles 5 and 6 of the *SCM Agreement*. For example, an actionable subsidy found to cause adverse effects may be withdrawn within a period of six months in apparent compliance with Articles 7.8 and 7.9 thereof. However, if the implementing Member later enacts a replacement subsidy of a relatively similar nature, structure, design and operation as the older subsidy, then an Article 21.5 panel would be required to determine (a) whether the replacement subsidy is taken to comply with the recommendations and rulings, and (b) whether this new measure taken to comply – the replacement subsidy – is consistent with the covered agreements and does not cause adverse effects. Such an interpretation is necessary to avoid a Member simply withdrawing one subsidy and replacing it somewhat later with a similar subsidy.

19. In this case, the compliance Panel, under Article 7.8 of the *SCM Agreement* and Article 21.5 of the *DSU*, must first assess Brazil's claim that no measures taken to comply exist with respect to the period 21 September 2005 and 1 August 2006. Second, the compliance Panel must assess whether the United States took action constituting full removal of the adverse effects caused by the basket of three price-contingent and mandatory measures, or fully withdrew those measures. Third, the compliance Panel must determine whether the measure taken to comply, *i.e.*, the limited amendment of the FSRI Act of 2002, is inconsistent with Articles 5(c), 6.3(c) and 6.3(d) of the *SCM Agreement*. In this case, steps two and three above involve the same proof, *i.e.*, that Brazil suffers serious prejudice by reason of the collective effect of marketing loan and CCP subsidies.

[9] Appellate Body Report, *U.S. – Softwood Lumber IV (21.5)*, para. 67; Appellate Body Report, *U.S. – Shrimp (21.5)*, para. 87.

26. Could the parties explain whether they agree or disagree with the arguments of New Zealand in its Third Party Submission that Article 7.8 of the SCM Agreement has certain consequences for the burden of proof in an Article 21.5 proceeding? [Paragraphs 5.04-5.06 of the Third party Submission of New Zealand]

20. Brazil does not agree entirely with New Zealand's "burden of proof" arguments. In the particular circumstances of this case, the original panel found that the "basket" of marketing loan, Step 2, and CCP subsidies caused significant price suppression in the world market for upland cotton. However, the United States repealed one of those three measures – the Step 2 legislation in the FSRI Act of 2002. In view of these particular facts and as set out in Answer to Question 25, Brazil has the burden of demonstrating under Article 7.8 that the United States did not take appropriate steps to remove the adverse effects caused by the original basket of measures. Viewed from the Article 21.5 perspective, Brazil has the burden of demonstrating that the revised FSRI Act of 2002 providing for marketing loan and CCP subsidies and mandatory and price-contingent payments was a measure taken to comply that is inconsistent with Articles 5 and 6.3 of the *SCM Agreement.*

21. Where no changes to the basket of measures found to cause collectively adverse effects have been made, then a complaining member would have the right to proceed immediately to Article 7.9 of the *SCM Agreement* and Article 22.2 of the *DSU*. The rationale for this right is set forth in Brazil's answer to Question 24 above, *i.e.*, that Article 7.8, at a minimum, requires an implementing Member to take *some* action.

22. However, if *arguendo*, a complaining member was required to challenge in an Article 21.5 proceeding the fact that an *unchanged* basket of measures continued to cause significant price suppression, then Brazil agrees with New Zealand that it might be appropriate to permit the complaining Member to establish a *prima facie* case simply by demonstrating the absence of any change in the measures. Further, for the reasons set forth in Brazil's Answer to Question 30, a complaining party would be entitled to rely in an Article 21. 5 proceeding on the prior findings of a panel. This is particularly the case where the same basket of measures found to cause adverse effects continues to exist, unchanged, at the time of the Article 21.5 proceeding.

27. Could the parties comment on the following statement of the European Communities:

> **"The text of Article 7.8 of the *SCM Agreement* does not state expressly that a Member that has been requested by the DSB to implement its recommendations and rulings under Article 7.8 of the *SCM Agreement* has to *do* anything" (original emphasis)**

23. Brazil disagrees with this assertion of the European Communities for the reasons set forth in Brazil's Answer to Panel Questions 22, 24, and 25.

28. The parties present divergent views with respect to the relevant marketing year to be considered by the panel in its analysis of Brazil's serious prejudice claims.

> ***a) Could the parties explain what they consider to be the relevant legal considerations by which the Panel should be guided in determining whether MY 2005 or MY 2006 is the appropriate marketing year?***

24. In assessing the effects of marketing loan and CCP subsidies, the Panel should use the methodological tool of a "reference period."[10] The appropriate reference period is MY 2005, the last recent marketing year for which essentially complete data exists.[11] It may also be appropriate to use partial MY 2006 data where the data has particular indicia of reliability and credibility. However,

[10] Panel Report, *U.S. – Upland Cotton*, paras. 7.1195-1.1201.
[11] Panel Report, *U.S. – Upland Cotton*, para. 7.1198.

partial year data should be used with caution because historical data shows that there have been fairly significant shifts of prices, demand, supply based on a number of different factors.

25. The relevant legal considerations for selecting a representative period of time, or a "reference period," to assess the existence of serious prejudice were discussed by the original panel as follows:

> Article 5(c) and 6(c) of the *SCM Agreement* do not refer to any specific time period within which we must conduct our evaluation. … The Panel concurs with the United States assertion that MY 2002 is a relevant year for our serious prejudice inquiry. It represents a recent period for which essentially complete data exists. The identification of "significant price suppression" flowing from the "effect of the subsidy" calls for an evaluation of this effects-based phenomenon that cannot be conducted in the abstract. Rather, discerning adverse effects of subsidies seems to us to require reference to a recent historical period. We believe, however, that it is important for the establishment of "current" serious prejudice that such prejudice would be established to exist up to, and including, a recent point in time.[12]

26. The original panel also found that "consideration of developments over a period longer than one year [is] not necessarily required (at least for Articles 5(c) and 6.3(c))," but that a longer period "provides a more robust basis for a serious prejudice evaluation than merely paying attention to developments in a single year."[13]

27. As the original panel noted, there is no specific guidance for selecting a reference period for assessing price suppression claims. However, context for interpreting Article 6.3(c) is found in other provisions of Part III of the *SCM Agreement*. Paragraph 2 of Annex IV provides that in "determining whether the overall rate of subsidization exceeds 5 percent of the value of the product … the "12-month period, for which sales data is available, preceding the period in which the subsidy is granted" be used. Similarly, paragraph 5 of Annex IV provides that the "rate of inflation experienced in the 12 months preceding the month in which the subsidy is to be given" be used.

28. Article 6.4 of the *SCM Agreement* provides in respect of claims of displacement or impedance under Article 6.3(b) that "an appropriate *representative period* sufficient to demonstrate clear trends in the development of the market for the product concerned … in normal circumstances, shall be at least one year." Article 6.7 refers to "the relevant period" for the purpose of Article 6.3(a) and 6.3(b) claims. Article 6.3(d) provides for the assessment of an increase in the world market share by comparing data from one year with "the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted." Less specific time periods are referred to regarding price undercutting claims under Articles 6.3(c) and 6.5 where the comparison of prices "shall be made … at comparable times."

29. These various provisions indicate that *some* period of time should be used to assess various forms of serious prejudice. While Article 6.3 provides for no particular time period for the assessment of significant price suppression, Brazil agrees with the original panel that significant price suppression in the same market requires an examination of some representative time period to assess trends, data, and evidence in order to conduct the necessary counter-factual analysis.

30. However, the use of such a "reference period" to determine whether serious prejudice exists, does not limit the "measures" at issue to that reference period. As Brazil demonstrated in its answers to Questions 11 and 15, challenges to subsidies causing serious prejudice are not "as applied" or "*per se*" claims. Rather, they are challenges based on the "effects" of "any subsidy." By contrast, the

[12] Panel Report, *U.S. – Upland Cotton*, para. 7.1198.
[13] Panel Report, *U.S. – Upland Cotton*, para. 7.1199.

United States seeks to turn the "reference period" for assessing serious prejudice into a jurisdictional limitation on the measures themselves. The United States is incorrect. The necessary use of a reference period has no implications for the implementation obligations of a subsidizing Member – and certainly does not limit those obligations to only payments made in the past during the reference period. Rather, the finding of adverse effects creates an implementation obligation to ensure that the use of the subsidy in the future does not cause adverse effects.

31. In sum, this compliance Panel should use the reference period of MY 2005 to assess whether serious prejudice exists from the new basket of measures. Partial MY 2006 data should also be used when it can be considered reliable and credible.

b) Do the parties agree or disagree with the argument of the European Communities that in a dispute involving a claim of present serious prejudice the parties must provide the "most recent reasonably available" data? [Paragraphs 43 and 54-55 of the Third Party Submission of the European Communities]

32. Brazil disagrees with European Communities to the extent that the European Communities asserts that panel considering serious prejudice challenges should rely on any partial year data simply because it is the most recent, regardless of its reliability in allowing an assessment of trends. As set out in Brazil's answer to Question 28(a), above, in assessing the effects of marketing loan and CCP subsidies, the compliance Panel should use the methodological tool of a "reference period."[14] The appropriate reference period is MY 2005, the last recent marketing year for which essentially complete data exists.[15] However, to assess effects, the compliance Panel can also use data throughout the lifetime of the FSRI Act of 2002. This permits the Panel to assess the continued relevance of the numerous findings of fact made by the original panel based on the earlier reference period MY 2002 and MY 1999-2002. The data to be assessed includes annual marketing year data regarding planted and harvested acreage, yields, production, exports, various futures and actual prices, production costs and the magnitude of subsidies in a given marketing year. Single week, month, or even partial year data do not provide as clear a picture because data on supply, demand, exports, prices, and price-contingent subsidies changes over time.

33. However, the reference period could be expanded to allow the assessment of evidence after the end of MY 2005. This is particularly the case given the fact that marketing loan and CCP programs in the FSRI Act of 2002 result in an unending stream of price-contingent subsidies that cause, with no clear dividing line, present serious prejudice today and a threat thereof tomorrow, and in the years ahead. Mandated marketing loan and CCP subsidies are paid today, and will continue to be paid months from now when the compliance Panel issues its report. In fact, current projections by USDA indicate that they will be paid every day until the FSRI Act of 2002 is repealed. Brazil's various serious prejudice claims in this proceeding, as before the original panel, involve past, present and future serious prejudice from this unending river of subsidies mandated by the FSRI Act of 2002. It is, therefore, appropriate for the compliance Panel to assess, with caution and only where it finds it credible and reliable, evidence concerning reference periods *after* 31 July 2006.

Questions to the United States

29. Does the United States contest the fact that a "strong positive relationship between upland cotton (base acre) producers receiving annual payments and upland cotton production" exists?[16] In particular, does the US disagree with the following statements[17]:

[14] Panel Report, *U.S. – Upland Cotton*, paras. 7.1195-1.1201.

[15] Panel Report, *U.S. – Upland Cotton*, para. 7.1198.

[16] See para. 131 of Brazil's First Submission. The Panel clarifies that this phrase refers to the fact that "the recipients who hold upland cotton base acres" and "those who continue to plant upland cotton" overlap with

- *a very large proportion of farms with upland cotton base acres continue to plant upland cotton in the year of payment;*

- *the overwhelming majority of farms enrolled in the programs which plant upland cotton also hold upland cotton base?*

Question to Brazil

30. How does Brazil respond to the argument of the United States that "whether or not the marketing loan and counter-cyclical payment programs or payments under the programs cause significant price suppression is a question of first impression"? [Rebuttal Submission of the United States, paragraph 219]

34. Brazil agrees that it is a question of "first impression" whether the new basket of price-contingent subsidy measures – consisting of marketing loan and CCP subsidies – causes significant price suppression in the world market for upland cotton. The original panel made its overall price suppression and causation findings largely based on the collective effects of the "basket of measures" that included Step 2, marketing loan, and CCP subsidies.

35. But this does not mean, as the United States argues, that all findings of the original panel regarding the individual effects of marketing loan and CCP subsidies, or even some of the collective effects of the original basket of measures are irrelevant. Brazil fully agrees with the United States that the original panel's findings "are taken as a given for purposes of this Article 21.5 proceeding."[18] As the Appellate Body stated, a compliance panel should apply the findings of the original panel "in the absence of any change in the underlying evidence in the record and explanations."[19]

36. In making a new assessment of whether marketing loan and CCP subsidies collectively cause serious prejudice, the compliance Panel can and must rely on the many findings of the original panel that isolated and examined *separately* the text, nature, magnitude, and effects of marketing loan and CCP subsidies.[20] The statutory and regulatory framework of these subsidies has not changed. Other unchanged findings involve the existence of Brazilian and U.S. cotton in the same world market, the continued relevance of the large world market share of U.S. supply, and the resulting substantial proportionate influence of U.S. production and exports on the world market price for cotton. Because the conditions of competition have not changed in any fundamental way since the original panel's reference period of MY 2002, the compliance Panel should rely on these earlier findings in making its new assessment of whether marketing loan and CCP subsidies cause significant price suppression in the world market for upland cotton.

2. The structure, design and operation of the countercyclical and marketing loan payment programs

Question to the United States

31. Brazil claims that the structure, design and operation of US counter-cyclical payments stimulate US upland cotton production. Both Brazil and the United States have referred to the

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each other to a great extent. (See para. 7.637 of the report of the original panel.) The Panel understands that Brazil uses this phrase in the same sense.

[17] These passages are reproduced from para. 7.636 of the report of the original panel.

[18] U.S. First Written Submission, para. 180.

[19] Appellate Body Report, *U.S. – Softwood Lumber VI (21.5)*, para. 103.

[20] Brazil First Submission, Sections 7.3 and 7.8; Brazil's Rebuttal Submission, Section 2.3.1.

Westcott (2005)[21] *study to provide support for their opposing analysis of the possible production impact of counter-cyclical payments. In its rebuttal, Brazil quotes the following passage from Westcott:*

> So where do CCPs fit compared with other farm commodity programs in the 2002 Farm Act? Marketing loans are fully coupled since they are available on all production and their link to market prices means they affect production decisions of farmers. Direct payments are mostly decoupled, since they are paid on a fixed, historically-based quantity rather than on current production and are not dependent on market prices or other factors that would affect production. …
>
> CCPs fall in between these two programs, having some properties similar to mostly decoupled direct payments and other properties similar to fully coupled marketing loans. Like direct payments, CCPs do not depend on current production since they are paid on a fixed, historically-based quantity. However, similar to marketing loans, CCPs are linked to market prices so there may be some influence on current production decisions of farmers, which would potentially make CCPs at least partially or somewhat coupled.

a) Does the United States agree with this characterization of the CCP?

b) How would the United States respond to the argument that, by design, counter-cyclical payments are in some measure coupled to production decisions because part of the payments is contingent on the actual realization of market prices?

3. Economic simulation model

Question to the United States

32. Brazil has presented a partial equilibrium model to simulate the effects of eliminating US upland cotton payments, particularly the marketing loan and counter-cyclical payments. In both its submission and rebuttal, the United States has provided reactions to the simulation model.

a) Would it be accurate to describe the United States' response as constituting a general acceptance of the framework of analysis adopted by Brazil but contesting the assumptions made regarding the values of the parameters, the supply and demand elasticities and the "coupling factor", used in the model? (The coupling factor is the amount by which the expected price is increased by each dollar per unit of subsidy payments.)

b) In its First Written Submission and Rebuttal Submission, the United States uses the same value of 1 that Brazil adopts for the coupling factor assigned to marketing loan payments. Does this imply an acceptance by the United States that, by design, marketing loan payments provide a one-for-one incentive to upland cotton production?

c) In its First Written Submission and Rebuttal Submission, the United States used a non-zero value of 0.25 (not much lower from the 0.4 that Brazil adopts) for the coupling factor assigned to counter-cyclical payments. Does this imply an acceptance by the United States that, by design, counter-cyclical payments are partially tied to upland cotton production, and of a magnitude (25 cents to a dollar of

[21] Paul A. Westcott, "Counter-Cyclical Payments Under the 2002 Farm Act: Production Effects Likely to be Limited" (Exhibit US-35).

counter-cyclical payments) not very far from Brazil's own estimate (of 40 cents to a dollar of counter-cyclical payments)?

E. EXPORT CREDIT GUARANTEES

1. Permissibility of an *a contrario* interpretation of item (j) of the Illustrative List

Questions to the United States

33. Please discuss whether (and if so, how) the panel rulings in Korea – Vessels and Brazil - Aircraft (21.5) (I and II) affect the United States' approach to the interpretation of the relationship between item (j) of the Illustrative List and Article 3.1(a) of the SCM Agreement.

34. Does the United States considers that item (j) of the Illustrative List is one of the provisions to which footnote 5 of the SCM Agreement applies? What impact does this have for the United States' interpretation of the interaction between item (j) of the Illustrative List and Article 3.1(a) of the SCM Agreement?

35. How does the United States address Brazil's argument that permitting an a contrario reading of item (j) would prevent a Member from challenging specific export credit guarantees or cohorts of such guarantees granted by a Member, as opposed to export credit guarantee programs? [see paragraphs 472 ff. of Brazil's Rebuttal]

Questions to Brazil

36. What is Brazil's reading of the Appellate Body's statement in paragraph 80 of its Report in Brazil – Aircraft (21.5) that it "... would have been prepared to find that the payments made under the revised PROEX are justified under item (k) of the Illustrative List"? Should the Panel take this statement into account in deciding whether item (j) can be interpreted a contrario?

37. Brazil has explained that, in its view, footnote 5 of the *SCM Agreement* expressly identifies the only circumstances in which the Illustrative List can be relied upon to identify measures that are not prohibited—namely, where the measures are "referred to…as not constituting export subsidies." This is also the view adopted, after extensive analysis, by the panels in *Brazil – Aircraft (21.5)* and *Korea – Vessels*, the latter of which concluded on this basis that item (j) of the Illustrative List does not meet the requirements of footnote 5 and therefore cannot be interpreted *a contrario*.

38. This position is not inconsistent with the Appellate Body's statement, in *dicta* in *Brazil – Aircraft (21.5)*, that it "would have been prepared," in effect, to accept an *a contrario* reading of the first paragraph of item (k) of the Illustrative List.[22]

39. As a threshold matter, it must be noted that the Appellate Body's statement appeared in *dicta*, and was accompanied by an express reservation that the Appellate Body did *not* purport to interpret or apply footnote 5 to this question. The Appellate Body was very clear on this point: "[W]e wish to emphasize that we are not interpreting footnote 5 of the *SCM Agreement*, and we do not opine on the scope of footnote 5…"[23] Accordingly, the analysis of footnote 5 by the panel in *Brazil – Aircraft (21.5)* and, subsequently, by the panel in *Korea – Vessels*, stands unaffected by the Appellate Body's statement. The *Korea –Vessels* panel expressly considered the Appellate Body's statement on

[22] Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 80.
[23] Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 80 (emphasis added).

item (k), first paragraph. It concluded that that statement posed no bar to the panel's analysis, which relied on footnote 5 to preclude an *a contrario* reading of item (j).[24]

40. Furthermore, item (k) is substantively distinct from other Illustrative List items. That is, even if the Appellate Body could be understood to have contemplated a possible *a contrario* reading of the first paragraph of item (k) notwithstanding footnote 5, such license would not extend beyond item (k).

41. As Brazil explained to the original panel[25], the first paragraph of item (k) is not like item (j). Paragraph 1 of item (k) calls for an analysis of "material advantage," which is closely related to the "benefit" standard under Article 1.1.[26] Both focus on an assessment of the "benefit to the recipient." An *a contrario* reading of the first paragraph of item (k) would not supplant the "benefit to recipient" standard in Article 1.1(b).

42. Not so with an *a contrario* reading of item (j). A determination that an ECG program breaks even tells one nothing about whether ECGs confer benefits on recipients relative to market benchmarks. Yet an *a contrario* application of item (j) would definitively eliminate any consideration of that "benefit". As such, it cannot be contemplated, whether or not an *a contrario* application of item (k), first paragraph, might conceivably be available.

43. Again, however, Brazil does not understand the Appellate Body's statement in *Brazil – Aircraft (21.5)* to have embraced an *a contrario* reading of item (k), because the Appellate Body did not carry out an analysis addressing the impact of footnote 5 on that question. To the contrary, the Appellate Body insisted that it was not taking that step, leaving the question entirely open to this compliance Panel.

2. Outstanding export credit guarantees / measures taken to comply

Questions to Brazil

37. Brazil relies on the panel and Appellate Body Reports in Brazil – Aircraft (21.5) in support of its arguments that the United States has not "withdrawn" the subsidy and is, "[a]t a minimum... prohibited from making 'payments' on claims against" any outstanding export credit guarantees [Paragraph 397 of Brazil's Rebuttal Submission]. Please discuss how the findings of the panel and Appellate Body in that case apply to the provision of the US export credit guarantees at issue.

44. Brazil's claim is supported by two elements of the compliance panel and Appellate Body reports in *Brazil – Aircraft (21.5)*.

45. First, these reports concluded that in continuing, after the implementation deadline, to perform on financial commitments undertaken before adoption of the DSB's recommendation, Brazil was not fully withdrawing the subsidy.[27] Analogously, in continuing, after the implementation deadline, to perform on ECGs issued before adoption of the DSB's recommendation, the United States has not fully withdrawn the subsidy.

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[24] Panel Report, *Korea – Commercial Vessels*, para. 7.197.

[25] Panel Report, *U.S. - Upland Cotton*, Annex I-1 (Answers of Brazil to Questions from the Panel, 11 August 2003), paras. 143-149.

[26] Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 61 ("We ruled [...] that the determination of whether a payment is 'used to secure a material advantage' calls for a comparison between the export credit terms available under the measure at issue and some other 'market benchmark'.").

[27] Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 45. *See also* Panel Report, *Brazil – Aircraft (21.5)*, para. 6.17. The compliance panel considered that "the obligation to cease performing illegal acts in the future is a fundamentally prospective remedy." Panel Report, *Brazil – Aircraft (21.5 I)*, para. 6.15.

46. Second, continuing to perform on ECGs outstanding on 1 July 2005 does not satisfy the definition of "withdraw" offered by the Appellate Body in *Brazil – Aircraft (21.5)*. The original panel found that the ECG programs were export subsidies within the meaning of item (j). The recommendation that the United States "withdraw the subsidy" therefore applied to the ECG programs. However, the recommendation also includes the subsidiary obligation not to perform on certain outstanding ECGs issued under those programs (*i.e.*, those ECGs issued for export transactions involving unscheduled products and rice).[28] The Appellate Body defined the term "withdraw" as to "remove" or "take away" the subsidy.[29] Paying a claim on default of a GSM 102 credit subject to the DSB's recommendation to "withdraw the subsidy" does not "remove" or "take away" that subsidy.

3. "Benefit" under Articles 1 and 3.1(a) of the *SCM Agreement*

Question to the United States

38. Please discuss the relevance of the original panel's characterization, in paragraph 6.31 of its report, of Brazil's reliance on Articles 1 and 3.1(a) of the SCM Agreement as "not a separate claim, but merely another argument" on the United States' view in this respect (and notably the United States statement, in paragraph 67 of its First Written Submission, that "... the panel in the original proceeding specifically declined to address Brazil's alleged 'claim' under Articles 1 and 3.1(a) of the SCM Agreement")?

Questions to Brazil

39. The Panel understands the United States to argue that it has relied on the Panel's findings under item (j) to implement the DSB recommendations with respect to export credit guarantees. How would this, in Brazil's view, affect the compliance panel's role in this proceeding? Was the United States also expected to implement changes in order to make its export credit guarantee programs consistent with article 1.1 and 3.1(a) of the SCM Agreement, even though there were no findings of the original panel in this respect?

47. The United States' "reliance" on the original Panel's findings under item (j) should not affect the compliance Panel's role in these Article 21.5 proceedings.

48. The United States cannot escape the export subsidy disciplines of the *Agreement on Agriculture* and the *SCM Agreement* by arguing that it somehow relied on the factual and legal basis for the original panel's finding that the GSM 102 program constitutes an export subsidy – to wit, item (j) of the Illustrative List. The question in these compliance proceedings is not limited to whether the United States has cured the basis on which the original panel found a violation. The Appellate Body has stated that in Article 21.5 proceedings, "a panel is not confined to examining the 'measures taken to comply' from the perspective of the claims, arguments and factual circumstances that related to the measure that was the subject of the original proceedings."[30]

49. Brazil thus understands that the compliance Panel is charged with reviewing the "new" measure – the amended GSM 102 program – from the perspective of the claims and arguments (as well as the facts) put before it in these proceedings, and not the claims and arguments before it in the original proceedings, with respect to the "old" measure.

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[28] Appellate Body Report, *U.S. – FSC (21.5)*, paras. 223-231 (recommendation to withdraw a subsidy in the form of an overarching measure, the FSC, includes the obligation to stop making pre-committed payments to existing FSCs); Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 45 ("… to continue to make payments under an export subsidy measure found to be prohibited is not consistent with the obligation to 'withdraw' prohibited export subsidies, in the sense of 'removing' or 'taking away'.").

[29] Appellate Body Report, *Brazil – Aircraft (21.5)*, para. 45.

[30] Appellate Body Report, *Canada – Aircraft (21.5)*, para. 41. *See also Id.*, para. 40.

50. Moreover, the United States could not legitimately have "relied on" the original panel's findings under item (j) as the bounds of its implementation obligations. The United States is surely aware that under the Appellate Body's interpretation of Article 21.5, any U.S. "measure taken to comply" would be a new measure subject to review from the perspective of claims, arguments and factual circumstances that may differ from the original proceedings. This new measure must be fully consistent with every relevant provision of the covered agreements.

51. In fact, in the original proceedings, Brazil urged the original panel to make findings on Brazil's extensive evidence and argument that under the "old" measure, GSM 102 ECGs confer "benefits" and constitute export subsidies under Articles 1.1 and 3.1(a) of the *SCM Agreement*.[31] While Brazil repeatedly urged it not to do so[32], the original panel exercised judicial economy with respect to the evidence and argument offered by Brazil under Articles 1.1 and 3.1(a). Nonetheless, the arguments are familiar to the United States, and should have been anticipated.

52. As emphasized in Brazil's oral statement at the meeting with the compliance Panel, all of this is not to say that the DSB's recommendations are irrelevant in implementation proceedings implicating prohibited subsidies and Article 4.7 of the *SCM Agreement*. As noted by the Appellate Body, "full *withdrawal* of a prohibited subsidy within the meaning of Article 4.7 of the *SCM Agreement* cannot be achieved by a 'measure taken to comply' that replaces the original subsidy with yet another subsidy found to be prohibited."[33]

53. Thus, even if the United States has withdrawn the elements of the GSM 102 program that made it an export subsidy under item (j) (a proposition with which Brazil does not agree), it has "replace[d] the original subsidy with yet another" prohibited subsidy – the provision of export-contingent GSM 102 ECGs at below-market fees. It has, therefore, failed to achieve "full withdrawal" of the subsidy, consistent with the Article 4.7 recommendation. In urging the Panel not to examine whether its replacement measure confers export-contingent "benefits", the United States seeks precisely to escape its obligation under that provision to fully withdraw the prohibited subsidy.

40. In paragraph 410 of its Rebuttal, Brazil refers to paragraph. 7.398 of the Panel Report in Canada – Aircraft II. The Panel notes, however, that in the same paragraph, the Canada – Aircraft II panel also indicated that there would be a "'benefit' when the cost-saving for a Bombardier customer for securing a loan with an IQ loan guarantee is not offset by IQ's fees". Please discuss, in light of this sentence, whether the Panel should read the Canada – Aircraft II panel as having rejected the "total cost of funds" as the proper benchmark under Article 14(c) of the SCM Agreement.

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[31] In addition to Brazil's exhibits in the original proceedings, *see* Brazil's 18 February 2004 Comments on U.S. Answers to Additional Questions, para. 65 (Panel Report, *U.S. – Upland Cotton*, Annex I-20); Brazil's 28 January 2004 Comments on U.S. Answers to Questions, paras. 139-144 (Panel Report, *U.S. – Upland Cotton*, Annex I-13); Brazil's 20 January 2004 Answers to Additional Questions, para. 14 (Panel Report, *U.S. – Upland Cotton*, Annex I-10); Brazil's 18 November 2003 Further Rebuttal Submission, *U.S. – Upland Cotton*, paras. 229-242; Brazil's 7 October 2003 Oral Statement, *U.S. – Upland Cotton*, para. 72; Brazil's 27 August 2003 Comments on U.S. Rebuttal Submission, paras. 68-80 (Panel Report, *U.S. – Upland Cotton*, Annex D-3); Brazil's 22 August 2003 Rebuttal Submission, *U.S. – Upland Cotton*, paras. 102-107; Brazil's 11 August 2003 Answers to Questions, paras. 139-140, 152-157, 182-189, 192-196 (Panel Report, *U.S. – Upland Cotton*, Annex I-1); Brazil's 22 July 2003 Oral Statement, *U.S. – Upland Cotton*, para. 116; Brazil's 24 June 2003 First Submission, *U.S. – Upland Cotton*, paras. 287-294.

[32] *See* Brazil's 2 November 2004 Other Appellant Submission, *U.S. – Upland Cotton*, para. 19; Brazil's 17 May 2004 Interim Comments, *U.S. – Upland Cotton*, paras. 19-23; Brazil's 28 January 2004 Comments on U.S. Answers, para. 145 (Panel Report, *U.S. – Upland Cotton*, Annex I-13); Brazil's 18 November 2003 Further Rebuttal Submission, *U.S. – Upland Cotton*, para. 228; Brazil's 11 August 2003 Answers to Questions, para. 150 (Panel Report, *U.S. – Upland Cotton*, Annex I-1).

[33] Appellate Body Report, *U.S. – FSC (21.5 II)*, para. 83 (italic emphasis in original; underlining supplied).

54. The sentence quoted by the compliance Panel from the report in *Canada – Aircraft Credits and Guarantees* appears to be a rough approximation of what the United States characterizes as a "total cost of funds" approach to Article 14(c).[34] Brazil does not believe that the panel in that dispute rejected the "total cost of funds" approach, or Article 14(c) in general, in subsequently concluding that "it is safe to assume that such cost difference would not be covered by [guarantee] fees if it is established that [the guarantee] fees are not market-based."[35] Rather, consistent with the proper interpretation of the provision, the panel merely declined to apply it rigidly, without consideration of the factual circumstances at hand.

55. At the United States' urging, the Appellate Body has rejected a "rigid" approach to the quantification methodologies included in Article 14, even for disputes regarding countervailing measures, to which the provision expressly applies. Quoting from a U.S. submission, the Appellate Body in *U.S. – Softwood Lumber IV* noted "that the use of the term 'guidelines' in Article 14 suggests that paragraphs (a) through (d) should not be interpreted as 'rigid rules that purport to contemplate every conceivable factual circumstance'."[36] Absent flexibility in Article 14, the Appellate Body worried that "the subsidy disciplines in the *SCM Agreement* . . . could be undermined or circumvented."[37]

56. *Canada – Aircraft Credits and Guarantees* was an export subsidy dispute under Part II of the *SCM Agreement*, to which Article 14 applies, but as context for a conclusion that Article 1.1(b) involves a "benefit to recipient", rather than a "cost to government", standard.[38] As noted above, even in the context of *countervailing measures* disputes, Article 14 admits of flexibility; the Appellate Body has cautioned against applying the provision too rigidly, without reference to the particular factual circumstances at hand. *Outside* the context of countervailing measures disputes, the *SCM Agreement* does not mandate that the existence of a "benefit" under Article 1.1(b) be established using a particular quantification methodology. Indeed, unlike in countervailing duty proceedings, where a duty must be calculated, disputes under Part II of the *SCM Agreement* do not require precise quantification of the "benefit" found under Article 1.1(b).

57. Thus, while the panel in *Canada – Aircraft Credits and Guarantees* was correct in acknowledging the relevance of the "total cost of funds" approach in Article 14(c) at some level, declining to follow it rigidly was entirely appropriate in the factual circumstances of that dispute. Unlike in countervailing duty proceedings, where a duty must be calculated as a function of the amount of "benefit" conferred by government support, no such precise calculation of the "benefit" flowing from government support is required for an export subsidy dispute. In *Canada – Aircraft Credits and Guarantees*, all Brazil, as the complaining Member, was required to show, was that *some* "benefit" was conferred. The panel in that dispute concluded that *some* "benefit" would have been conferred were fees for the government guarantee to be shown to be below-market.[39] Doing so did not constitute "rejection" of Article 14(c), but instead, was consistent with the proper interpretation of Article 14, and constituted a flexible approach called for by the factual circumstances at hand.

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[34] U.S. First Written Submission, para. 138.

[35] Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.345.

[36] Appellate Body Report, *U.S. – Softwood Lumber IV*, para. 92. *See also* U.S. Appellant's Submission, *U.S. – Softwood Lumber IV*, para. 25, accessed February 2007 at http://www.ustr.gov/assets/Trade_Agreements/Monitoring_Enforcement/Dispute_Settlement/WTO/Dispute_Settlement_Listings/asset_upload_file760_6326.pdf ("[T]he provisions of Article 14 are explicitly designated as "guidelines" and they must be interpreted in accordance with the ordinary meaning of that word. A "guideline" is "a directing or standardizing principle laid down as a guide" to procedure or policy. The fact that Members are obligated to follow the guidelines in Article 14 does not alter their character. Members have specifically designated the provisions in Article 14 as "guides" or "principles," not rigid rules that purport to contemplate every conceivable factual circumstance.").

[37] Appellate Body Report, *U.S. – Softwood Lumber IV*, para. 100.

[38] Appellate Body Report, *Canada – Aircraft*, para. 155.

[39] Panel Report, *Canada – Aircraft Credits and Guarantees*, para. 7.345.

Questions to both parties

41. What are the relevant considerations to guide the Panel in the selection of a market benchmark in this case?:

a) That the institution that provides the product is, on the whole, or on a program or product-specific basis, profitable? If so, is "any" profit sufficient to qualify an institution/product/program as a relevant "market benchmark" or must the institution/product/program achieve a certain level of profit? Must the Panel conduct an examination of the level of profit achieved by commercial or private actors operating in the field?

b) Are the institution/program/products' stated goals relevant in assessing whether they can be used as a "market benchmark"?

***c)* Is the "governance" of the institution relevant?**

d) What other factors are relevant?

58. When assessing a benchmark drawn from an entity that is truly a participant in the "marketplace"[40] – meaning an entity the financial independence of which is not "[]distorted by government intervention"[41] – a panel need not review the entity's profitability, goals or governance. If the entity is truly a participant in the marketplace, the terms on which it offers its products *are* the market, by definition. In those circumstances, it is not relevant for a panel to inquire into the entity's profitability, goals or governance (unless those elements are alleged to reveal that the entity is not truly a participant in the marketplace).

59. In these proceedings, Brazil has demonstrated that there is no credit protection product available in the marketplace that is comparable to a GSM 102 ECG.[42] Accordingly, the GSM 102 program offers a unique financial instrument without any parallel at market, and therefore confers "benefits" *per se*. Where other Members' measures were at issue, the United States has agreed.[43]

60. In addition, Brazil has offered evidence demonstrating that GSM 102 fees are considerably below those charged for virtually identical products offered by an entity that is not a participant in the marketplace – the U.S. Export-Import Bank ("ExIm Bank"). Benchmarking to fees charged by an entity that is not a participant in the marketplace likely understates the extent of the "benefit" conferred by a GSM 102 ECG, for reasons expressed in Brazil's submissions to the compliance Panel.[44] In the circumstances of these particular proceedings, Brazil is willing to accept that understatement. The Panel will recall that in a prohibited subsidies dispute, unlike in a countervailing measures dispute, quantification of the precise amount of "benefit" is not required.

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[40] Appellate Body Report, *Canada – Aircraft*, para. 157 ("In our view, the marketplace provides an appropriate basis for comparison in determining whether a 'benefit' has been 'conferred', because the trade-distorting potential of a 'financial contribution' can be identified by determining whether the recipient has received a 'financial contribution' on terms more favourable than those available to the recipient in the market.").

[41] Panel Report, *Brazil – Aircraft (21.5 II)*, para. 5.29.

[42] Brazil's First Written Submission, paras. 377-378. *See also Id*., Annex III (Statement of Professor Rangarajan Sundaram), paras. 8-9.

[43] Panel Report, *Canada – Aircraft Credits and Guarantees*, Annex C-2 (para. 7) ("If the commercial market does not offer a particular borrower the exact terms offered by a government, then the government is providing a benefit to the recipient whenever those terms are more favorable than the terms that are available in the market. A government entity "operating on commercial principles" is still a government entity. It is not the commercial market.").

[44] *See, e.g.*, Brazil's Oral Statement, paras. 188-192.

61. In a dispute under Part II of the *SCM Agreement*, a defending Member may not, however, justify the terms on which it offers a challenged financial contribution with reference to a benchmark associated with a product offered by a government/public entity. Brazil believes that the compliance Panel's question is whether, in these circumstances, the defending Member could appeal to the profitability, goals or governance of that government/public entity, to show that even if the *entity* is not truly a participant in the marketplace, the *product* serving as the proposed benchmark is offered on market terms.

62. In Brazil's view, the answer must be in the negative, to avoid circumvention of the disciplines in the *SCM Agreement*.

63. Brazil addressed the issue of "profitability" of a government/public entity in its opening statement at the meeting with the compliance Panel.[45] The original panel in this dispute observed that public entities tend to borrow from government treasuries, or enjoy a guarantee flowing from the full faith and credit of governments.[46] As a result, government/public entities tend to enjoy a lower cost of funds than their market-based counterparts. Other immunities enjoyed by government/public entities – from taxation, in particular – lower costs even further.[47] The United States made this point forcefully in *Canada – Aircraft Credits and Guarantees*:

> . . . [T]he competitive pressures on financial actors in the marketplace generate financing offers that reflect any internal cost advantages enjoyed by a particular actor. For wholly commercial actors, however, the ability and willingness to compete is constrained by such factors as balance sheets, true market-determined borrowing costs, arms-length shareholder lending policies, arms-length business costs, and the disciplines imposed by the need to provide returns to owners. [Government/public entity's] operations are largely free of these constraints, and thus are in a position to confer benefits by exceeding, if sometimes only in a small way, what purely market-based financial institutions can (or may be willing to) offer. Their ability to do so explains their existence, since there would otherwise be no reason for [government/public entity operations] to exist in parallel with private financial market actors, much less any logical reason for governments to limit their [entities'] activities to nationals.[48]

64. Whatever the definition of the term, making a "profit" does not mean that fees charged by a government/public entity are consistent with market. A government/public entity can charge below-market fees and still make a "profit", particularly because its costs are below those faced by its market-based counterparts. A market-based entity must go a step further to survive: it must charge fees high enough to make a profit on costs higher than those faced by its government/public counterpart, and the profit must offer a sufficient return to attract capital from investors. "Profitability" of a government/public entity does not provide a relevant or sufficient measure of the "benefit" conferred by a government financial contribution.

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[45] Brazil's Oral Statement, paras. 188-192. To show the conservative nature of its ExIm Bank exercise, Brazil has discussed the extent to which ExIm Bank is loss-making. *See* Brazil's First Written Submission, para. 384 and Annex III (Statement of Professor Rangarajan Sundaram), paras. 17-24. ExIm Bank's fees are apparently not high enough to turn a "profit" on the low cost of funds it enjoys as a U.S. government agency backed by the full faith and credit of the United States Treasury.

[46] Panel Report, *U.S. – Upland Cotton*, para. 7.858.

[47] Brazil's Rebuttal Submission, paras. 439 (IFC immune from taxation), 441 (EBRD immune from taxation), 442 (IDB immune from taxation).

[48] Panel Report, *Canada – Aircraft Credits and Guarantees*, Annex C-2 (Third Party Submission of the United States), para. 5.

65. The United States made this point in the panel *Korea –Vessels*. The panel asked whether the United States considered it relevant, in assessing "benefit", that a Korean government bank, KEXIM, "operated at a profit". The United States responded as follows:

> No. … [T]he benefit-to-recipient approach must be applied to KEXIM financing. That approach, in turn, requires a comparison of KEXIM financing to a market-based benchmark; *i.e.*, comparable commercial financing. Evidence that KEXIM earned a profit would be irrelevant to this exercise, because it would not prove that KEXIM was charging market rates.[49]

66. A government/public entity's stated goal of offering products consistent with market is equally irrelevant, as such a goal can be considered little more than self-serving. The governance of a government/public entity will tend, as noted by the original panel[50], to demonstrate access enjoyed by the entity to low-cost funds or government guarantees, which in turn highlight the irrelevance of the entity's ability to turn a profit.

4. Claims under item (j) of the Illustrative List

Questions to the United States

42. How does the United States address Brazil's arguments with respect to the MPRs under the OECD Arrangement?

Question to Brazil

43. What is Brazil's reaction to paragraph 25 of Japan's Third Party Submission?

67. As the Panel will recall, Brazil has demonstrated that fees charged by the United States in the GSM 102 program are significantly lower than the minimum premium rates ("MPRs") of the OECD Arrangement on Officially Supported Export Credits (the "OECD Arrangement") for similar risk categories, tenors and repayment profiles. Brazil offers this comparison as additional evidence that GSM 102 fees are not structured and designed to cover the long-term costs and losses of the program, because the OECD Arrangement MPRs are set with the objective of ensuring "that Participants…charge premium rates in addition to interest charges that…are not inadequate to cover long-term operating costs and losses."[51]

68. In paragraph 25 of its Third Party Submission, Japan objects to Brazil's invocation of the OECD Arrangement in this context. Japan's objections rest on the premise that the OECD Arrangement is factually inapposite for a comparison to GSM 102 ECGs, because the OECD Arrangement does not cover export credits for agricultural commodities such as upland cotton and it applies to export credits with different tenors than those offered under GSM 102.

69. Japan's objection appears to stem from a misunderstanding of the purpose for which Brazil has invoked the OECD Arrangement's MPRs. Brazil acknowledges these factual differences between the GSM 102 program and the OECD Arrangement, and indeed did so in its own submissions.[52] These distinctions, however, do not undermine the value of the comparison between GSM 102 fees

[49] Response of the United States to Questions from the Parties, *Korea – Measures Affecting Trade in Commercial Vessels*, 22 March 2004, paras. 6-7 (emphasis added), accessed February 2007 at http://www.ustr.gov/assets/Trade_Agreements/Monitoring_Enforcement/Dispute_Settlement/WTO/Dispute_Settlement_Listings/asset_upload_file769_5561.pdf.

[50] Panel Report, *U.S. – Upland Cotton*, para. 7.858.

[51] Exhibit Bra-547 (OECD Document TD/PG(2004)10/FINAL, 6 July 2004, para. 1).

[52] Brazil's First Written Submission, para. 442.

and the MPRs to this Panel's analysis under item (j). This is because Brazil does not contend that the OECD MPRs constitute a strict quantitative benchmark for analysis of the U.S. upland cotton ECG fees. Brazil is not, for example, proposing the kind of direct quantitative comparison that would be triggered under item (k), second paragraph, of the Illustrative List. Rather, this comparison offers the compliance Panel a *qualitative* reference point for appreciating the degree to which GSM 102 fees fall below internationally-accepted standards for ECG programs that are, according to the OECD, structured and designed to break even.

70. Brazil turns to Japan's specific objections. As Brazil explained in its First Written Submission, comparing GSM 102 fees for agricultural ECGs to the OECD MPRs for industrial ECGs is, if anything, conservative. As Japan itself notes, "the risks of financing arrangements" for agricultural products are "substantial." As Brazil has noted, the perishability of agricultural products diminishes their value as security for lenders.[53] Japan echoes Brazil's argument that in these circumstances, GSM 102's extended coverage is unique; Japan acknowledges that in normal circumstances, even non-market entities like ExIm Bank cap coverage under similar credit protection products "at 180 days for bulk agricultural products."[54] If the OECD Arrangement were to cover export credits for agricultural products, the MPRs would certainly not be lower; the gap between MPRs and GSM 102 fees would not decrease, and would likely increase.

71. Nor does Japan's objection concerning the divergence between tenors for credits covered by GSM 102 and credits subject to OECD MPRs undermine Brazil's reference to the latter, for two reasons.

72. First, although the OECD Arrangement formally covers export credits with a tenor of two years or more, it provides a formula that allowed Brazil to extrapolate the MPRs that *would be* applicable to export credit guarantees with terms of less than two years. This permits an "apples-to-apples" comparison with respect to fees for credits with tenors of less than two years.

73. Second, the comparison provided by Brazil spans GSM 102 ECGs with tenors ranging as long as 36 months.[55] Even if one were to accept a premise that GSM 102 fees may be compared only to MPRs for export credits with terms of two years or more, the comparison points at 24, 30 and 36 months would all remain valid.[56] Those points of comparison, in turn, reveal not only a wide gap between GSM 102 fees and MPRs, but a gap that grows as the tenor – and, correspondingly, the risk – of the transaction increases. This same pattern appeared in Brazil's comparison of GSM 102 fees and fees charged by the U.S. Export-Import Bank. As the risks of the transactions increase, the inadequacy of the GSM 102 fees as compared to the MPRs (or to ExIm's fees) becomes even more pronounced.

[53] Brazil's First Written Submission, para. 443.

[54] *See* Japan's Third Party Submission, para. 25, *citing* Brazil's First Written Submission, paras. 387, 389.

[55] Exhibits Bra-548 (MPR and CCC Annual Comparison) and Bra-549 (MPR and CCC Semi-Annual Comparison).

[56] *See* Exhibits Bra-548 (MPR and CCC Annual Comparison) and Bra-549 (MPR and CCC Semi-Annual Comparison).

74. Accordingly, Brazil maintains that a comparison of the fees charged in the GSM 102 program with the MPRs set under the OECD Arrangement constitutes a useful reference point for this compliance Panel. The factual differences noted by Japan in fact suggest that the reference point is a conservative one, such that it is even more clear that the GSM 102 program is not structured and designed to charge fees that cover its long-term operating costs and losses.