

**THE WTO LEGAL REGIME FOR THE ACTIONABILITY OF AGRICULTURAL
SUBSIDIES AFTER THE EXPIRY OF THE PEACE CLAUSE**

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DOCTORAL DISSERTATION

ABSTRACT

Because of the *Agreement on Agriculture's* (AoA) Article 13, dubbed the "Peace Clause," the challengeability of agricultural subsidies has been limited; Article 13 had the power to prevent several types of legal challenges. The Peace Clause has expired, and now many agricultural subsidies can be challenged under substantive provisions of the *General Agreement on Tariffs and Trade (GATT 1994)* and the *Agreement on Subsidies and Countervailing Measures (SCM Agreement)*. However, there has been some uncertainty, because the new arrangement of agricultural subsidies' challengeability is being defined by the interpretation and correlation of three different WTO agreements. This study verified, using a two-pronged method, that there is no conflict among the *GATT 1994*, the *SCM Agreement* and the *AoA*, and for this reason, they have to be applied together to regulate agricultural subsidies. This does not mean that all *SCM Agreement* provisions are automatically applied to agricultural subsidies, with a consequent free ride for challenges to agricultural subsidies. A successful challenge still has to overcome the *SCM Agreement's* higher thresholds for challengeability compared with those of the *GATT 1994* period. This condemnation became more difficult after the implementation of the WTO. Consequently, the goals established in the *AoA* of substantial and progressive reductions in agricultural support and protection still have to be accomplished.

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The LORD hath done great things for us; whereof we are glad. Psa. 126:3.

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TABLE OF CONTENTS

Introduction	1
CHAPTER I. The Legal System of Agricultural Subsidies Before the Uruguay Round	13
I.1 Background	13
I.1.1 Agricultural Subsidies in the <i>GATT 1947</i>	18
I.1.2 The <i>GATT</i> Legal Framework of Challengeability of Agricultural Subsidies	20
I.2 Subsidies under <i>GATT 1947</i> Article XVI	21
I.2.1 Domestic Subsidies and the Concept of “Subsidy” and “Serious Prejudice”	22
I.2.2 Export Subsidies and the Concept of “More Than an Equitable Share of the World Export Trade”	27
I.2.2.1 The Havana Charter	29
I.2.2.1.1 The <i>France - Wheat Exports</i> Case and the Concept of “More than an Equitable Share of the World Export Trade”	35
I.2.2.1.2 The <i>EC – Sugar Exports</i> Cases and the Link Between the Concept of “Equitable Share” and “Displacement” under the TRSC	40
I.3 The Tokyo Round	49
I.3.1 The Tokyo Round Subsidies Code and the Market-Effect Requirements	50
I.3.1.1 The <i>EEC – Wheat Flour Subsidies</i> Case and the Wrong Application of New Concepts of the TRSC, Such as “Price Undercutting”	60
I.3.1.2 The <i>EEC – Pasta Subsidies</i> Case and the Concept of “Primary Product”	67
I.4 Other Possibilities of Challengeability for Agricultural Subsidies under the <i>GATT 1947</i>	74
I.4.1 Countervailing Duties – <i>GATT 1947</i> Art. VI and TRSC Regulation	75
I.4.2. Nullification or Impairment of Any Benefit – <i>GATT 1947</i> Art. XXIII	87
I.4.2.1 <i>GATT 1947</i> Article II – Schedule of Concessions	88

I.4.2.1.1 <i>EEC – Oilseeds I</i> Case and the Threshold of Challengeability under <i>GATT 1947</i> Art. XXIII and XVI	92
I.4.3 <i>GATT 1947</i> Article III - National Treatment and Related Provisions	97
I.4.3.1 The <i>EEC - Canned Fruit</i> Case and the Concept of “Trade Damage”	100
I.5 The <i>GATT</i> Agenda for Agriculture before the Uruguay Round – the US Waiver and the Balance of Power	104
I.5.1 The US Waiver	104
I.5.1.1 The US – Dairy Case and the US Waiver	108
I.5.1.2 Canada – Eggs Case and the Weaknesses Caused the US Waiver	112
I.5.2 The Balance of Power During the <i>GATT</i> Years	113
I.6 Conclusion	116
I.6.1 Challengeability of Agricultural Subsidies Before the Peace Clause (<i>GATT</i> Legal Framework)	119
CHAPTER II The Legal Regime of Agricultural Subsidies – The Uruguay Round	122
II.1 The Transition from the <i>GATT</i> to the WTO	124
II.2 Agriculture in the WTO System	133
II.3 The <i>Agreement on Agriculture (AoA)</i>	135
II.3.1 The Peace Clause	136
II.3.1.1 The Background of the Peace Clause	136
II.3.1.2 Substantive Provisions	138
II.3.1.3 The Proliferation of Distortive Measures During the Peace Clause Period	145
II.3.2 The Specificity of the <i>Agreement on Agriculture</i>	148
II.3.2.1 The Agreement on Modalities	149
II.3.3 The <i>AoA</i> General Structure	150

II.3.3.1 Export Subsidies	151
II.3.3.2 Domestic Support	160
II.4 Challenges of Agricultural Subsidies during the Peace Period	170
II.4.1 The <i>United States – Subsidies on Upland Cotton</i> (DS 267)	179
II.4.1.1 The Novelty of the Case	181
II.4.1.2 The Figures of the Case	184
II.4.1.3 The Panel	186
II.4.1.4 The Peace Clauses’ Barrier to Challengeability	190
II.4.1.5 The Appeal	195
II.4.1.6 Compliance	198
II.5 The <i>Agreement on Subsidies and Countervailing Measures</i> [SCM Agreement]	202
II.5.1 Defining Boxes under <i>SCM Agreement</i> Challengeability	204
II.5.2 Definition of Subsidy	205
II.5.3 The Specificity Test	211
II.5.4 Serious Prejudice and Displacement	214
II.5.5 Countervailing Duties and the <i>SCM Agreement</i> Concept of Injury	222
II.6 Conclusion	225
II.6.1 Challengeability of Agricultural Subsidies under the Uruguay Round before the expiry of the Peace Clause	226
CHAPTER III. THE LEGAL REGIME FOR AGRICULTURAL SUBSIDIES AFTER THE EXPIRY OF THE PEACE CLAUSE	228
III.1 An Overview of Agriculture after the Uruguay Round	228
III.2 Legal Principles of Interpretation and the Relationship Among the <i>AoA</i> , <i>SCM Agreement</i> and <i>GATT 1994</i>	231

III.2.1 Applicable Principles of International Law	231
III.2.2 Applicable Principles of the World Trading System	236
III.2.3 Conflict among Agreements	241
III.2.3.1 The Theoretical Methodology to Identify Conflict	243
III.2.3.2 The Empirical Methodology to Identify Conflict	247
III.3 The Application of the Theoretical and the Empirical Methods to Identify Whether There Is Conflict among the <i>AoA</i> , <i>SCM Agreement</i> and <i>GATT 1994</i>	251
III.3.1 The Application of the Theoretical Method to Green Box Measures	251
III.3.2 The Theoretical Method Applied to Green Box Measures	257
III.3.3 The Empirical Method Applied to Non-Green Box Measures	260
III.3.4 The Theoretical Method Applied to Non-Green Box Measures	261
III.3.5 The Empirical Method Applied to Export Measures	263
III.3.6 The Theoretical Method Applied to Export Measures	264
III.4 The Cumulative Application of the <i>AoA</i> , <i>SCM Agreement</i> and <i>GATT 1994</i> to Define the “New” Limits of Challengeability for Agricultural Subsidies Upon the Expiry of the Peace Clause	266
III.4.1 The Actionability of Agricultural Subsidies under the <i>SCM Agreement</i>	267
III.4.1.1 Agricultural Subsidies and the <i>SCM Agreement</i> Definition of Subsidy	271
III.4.1.2 Specificity under the <i>SCM Agreement</i>	276
III.4.1.3 The Challengeability of Agricultural Subsidies under <i>SCM Agreement</i> Part II	280
III.4.1.4 The Actionability of Agricultural Subsidies under <i>SCM Agreement</i> Part III	282
III.4.1.4.1 Effect on the World Market Share and Displacement	287
III.4.1.5 Challengeability of Agricultural Subsidies under <i>SCM Agreement</i> Part V	290
III.4.2 Challengeability of Agricultural Subsidies under <i>GATT 1994</i>	294

III.5 The New Boundaries for the Challengeability of Agricultural Subsidies Upon the Expiry of the Peace Clause	299
III.5.1 Green Box Subsidies	300
III.5.2 Non-Green Box Subsidies	307
III.5.3 Agricultural Export Subsidies	312
CHAPTER IV. Conclusion	318
BIBLIOGRAPHY	324

LIST OF ABBREVIATIONS

- AB – Appellate Body
- AMS - Aggregate Measurement of Support
- AoA - Agreement on Agriculture
- BFA – Banana Framework Agreement
- CAP – Common Agricultural Policy
- CIF – Cost, Insurance and Freight
- DP – Direct Payments
- DSU – Dispute Settlement Understanding
- EC – European Communities
- ECG – Export Credit Guarantee Programs
- EEC – European Economic Community
- EEE – Export Enhancement Program
- EU- European Union
- EWG - Environmental Working Group
- FOB – Free on Board
- FSC – Foreign Sales Corporations
- GATT 1947 – General Agreement on Tariffs and Trade
- GATT 1994 - General Agreement on Tariffs and Trade
- ISA – International Sugar Agreement
- IMF – International Monetary Fund
- ITO – International Trade Organization
- ITS – International Trading System

IWA – International Wheat Agreement

LDA – Least Developed Countries

MFN – Most Favored Nation Principle

NGO – Non-Governmental Organization

NTB – Non-Tariff Barrier

OECD – Organisation for Economic Co-operation and Development

ONIC – Office National Interprofessionnel des Cereales

PFC - Production Flexibility Contract Payments

SCM Agreement – Agreement on Subsidies and Countervailing Measures

TNC – Trade Negotiations Committee

TR – Tokyo Round

TRQ – Tariff Rate Quota

TRSC – Tokyo Round Subsidies Code

US – United States of America

USDA – United States Department of Agriculture

UR – Uruguay Round

VCLT – Vienna Convention on the Law of the Treaties

VER – Voluntary Export Restraint Agreement

WB – World Bank

WTO – World Trade Organization

LIST OF ILLUSTRATIONS

Table 1: Rural-Urban Poverty Gap	15
Table 2: Share of Developing Countries' Exports in World Trade	16
Table 3: Challengeability of Agricultural Subsidies before the Expiry of the Peace Clause	119
Graphic 1: The Greening Shift of Domestic Support: EC Notifications at WTO from 1995 to 2002	146
Table 4: Product-Shifting in Market Access: Tariff Restrictions on Sensitive Agricultural Products in Specific Countries	147
Table 5: Challengeability of Agricultural Subsidies during the Peace Years	227
Frame 1: Theoretical Method – Four Types of Measures	246
Diagram 1: Theoretical Method – Conflicts of Norms	247
Diagram 2: Zone of Confluence of Challengeability of Agricultural Subsidies	299
Table 6: Challengeability of Green Box Subsidies After the Expiry of the Peace Clause	305
Table 7: Challengeability of Non-Green Box Subsidies After the Expiry of the Peace Clause	310
Table 8: Challengeability of Agricultural Export Subsidies After the Expiry of the Peace Clause	315
Table 9: Challengeability of Agricultural Subsidies Upon the Expiry of the Peace Clause	320

LIST OF ANNEXES

Annex I: The WTO Panel Process	344
Annex II: Countervailing Duties under the <i>SCM Agreement</i>	346
Annex III: Overview About the Negotiations of Agricultural Subsidies	355
Annex IV: Group of Countries and Alliances in the WTO Agricultural Negotiations	376
Annex V: Interview of Roberto Azevedo, the former chief of the Brazilian Mission at WTO in Geneva (16 October 2004) in Brazilian Ministry of Foreign Affairs, Brasilia	383

INTRODUCTION

In the World Trade Organization [WTO] there are three Agreements to regulate agricultural subsidies: the *General Agreement on Tariffs and Trade*¹ [*GATT 1994*], the *Subsidies and Countervailing Measures Agreement*² [*SCM Agreement*] and the *Agreement on Agriculture*³ [*AoA*]. In order to define the boundaries of the legal framework of agricultural subsidy regulation, it is necessary to define how these Agreements interrelate. Taking into account that these Agreements comprise the legal framework of agricultural subsidy regulation – not only their content, but also how they interrelate – a definition of the boundaries of this regulation is in order.

The *AoA* was one of the agreements that arose from the international trading system that was established in 1995 with the creation of the WTO. This Agreement contained substantive rules for agricultural subsidies. However, because *AoA* Art. 13, dubbed the “Peace Clause,” had

¹ *General Agreement on Tariffs and Trade 1994* [GATT]. *World Trade Organization. The Legal Texts. The Results of the Uruguay Round of Multilateral Trade negotiations* (Cambridge: Cambridge University Press, 1990) [*WTO Legal Texts*]. GATT 1947 is the predecessor of the WTO. During the Bretton Woods Conference, the idea of creating the International Trade Organization emerged as a part of the economic plan after the World War II. In 1950 the idea of the International Trade Organization [ITO] failed and the GATT 1947 remained; however, it was a treaty, not an international organization. Its main objectives were the reduction of international trade barriers, which was gradually being achieved through a series of agreements to reduce tariff barriers, quantitative restrictions and subsidies. In 1995, right after the end of the Uruguay Round [UR], the World Trade Organization was created and GATT 1995 was incorporated in the WTO regulations as one of the Agreements of Annex 1A that regulate trade in goods. The current GATT Agreement comprises the provisions of GATT 1947 – as modified by the terms of legal instruments that entered into force before the implementation of the WTO – along with the other provisions, protocols, explanatory notes and observations specified in the preamble of GATT 1994. For the purposes of this research, GATT 1994 will be referred as *GATT 1994*.

² The *SCM Agreement* came into force on the January 1, 1995, with the creation of the WTO, as one of the Annex 1A Agreements negotiated during the Uruguay Round (1986-1994). The Agreement defines subsidies and disciplines their use, besides regulating the actions other WTO Members can take to counter the effects of subsidies. *Agreement on Subsidies and Countervailing Measures* [*SCM Agreement*]. *WTO Legal Texts, supra* note 1.

³ The *AoA* also came into force on the January 1, 1995, with the creation of the WTO, as one of the Annex 1A Agreements negotiated during the Uruguay Round (1986-1994). It included commitments by all WTO Members to improve market access and reduce trading-distort subsidies in agriculture.

Those commitments were implemented over a period of six years (10 years for developing countries), starting in 1995. WTO Members agreed in 1999 to initiate negotiations to keep the agricultural reform process, which were incorporated into the Doha Round. *Agreement on Agriculture* [*AoA*]. *Ibid.*

the power to prevent several⁴ types of legal challenges⁵ the actionability⁶ of agricultural subsidies was limited.⁷

The Peace Clause expired on December 31, 2003, but the arrangement in the application and the interpretation of the *AoA*, *SCM Agreement* and *GATT 1994* Agreements to regulate the challengeability of agricultural subsidies is not automatic. There is no consensus on how to apply the *SCM Agreement* procedural provisions to *AoA* substantive regulation of agricultural subsidies.

The division of regulation of challengeability of agricultural subsidies by three (*AoA*, *SCM Agreement* and *GATT 1994*) created some uncertainties whose consequences were faced only after the expiry of the Peace Clause. Its expiry posed the relevant question of whether it is possible for an agricultural subsidy to comply with one WTO agreement and violate another. More specifically, even if agricultural subsidies comply with the *AoA* schedules, can they still be

⁴ *AoA* Art. 13 established that during the implementation period domestic subsidies that conformed to the provisions of Annex II of *AoA* should be non-actionable for countervailing duty purposes, exempted from actions under *GATT* Art. XVI, II and XXIII and *SCM Agreement* Part III; domestic subsidies that conformed to *AoA* Art. 6 should be exempted from countervailing duties unless there was injury or threat thereof, exempted from actions under *GATT* Art. XVI and *SCM Agreement* Articles 5 and 6 if there is no support in excess of what was decided in the marketing year of 1992 and exempted from actions under *GATT* Art. II and XXIII if there was no support in excess than what was decided in the marketing year of 1992; and export subsidies that conformed to Part V of the *AoA* and according to the Member's schedule should be subjected to countervailing duties or actions under *SCM Agreement* Part V only upon determination of injury or threat thereof and exempted from actions based on *GATT* Art. XVI and *SCM Agreement* Articles 3, 5 and 6.

⁵ Arts. 5 and 6 of the *SCM Agreement* did not apply to agricultural subsidies as provided on art 13 of the *Agreement on Agriculture*.

⁶ The term actionability means any challenge of agricultural subsidies under the WTO system. If a subsidy can be actionable, it does not necessarily mean it is illegal. The Peace Clause used to constrain actionability, but did not regulate legality. However, *SCM Agreement* Part III specifically defines *Actionable Subsidies* as subsidies that cause *adverse effects* (injury, nullification or impairment of benefits and serious prejudice) to another Member. Therefore this study will use the word *challengeable* to refer to any challenge of agricultural subsidies under the WTO system and the word *actionable* to refer to actionable subsidies of *SCM Agreement* Part III only.

⁷ "Art. 13 of the *WTO Agreement on Agriculture*, known as the 'Peace Clause', precluded most of WTO dispute settlement challenges against a country that is complying with the Agreements' liberalization commitments." Richard H. Steinberg & Timothy E. Josling, "When the Peace Ends: The Vulnerability of EC and US Agricultural Subsidies to WTO Legal Challenge" (2003) 6 *Journal of International Economic Law* 1 [Steinberg, "Peace Clause"]. "The WTO's "Peace Clause" *Agreement on Agriculture* Art. 13, during its effective period, has prevented most of types of legal challenges to most Agricultural Subsidies". John R. Magnus, "The Evils of a Long Peace: Legal Consequences of WTO "Peace Clause", Expiry and Practical Issues for New Litigation over Farm Subsidies" *Global Business Dialogue*, (Paper presented to the Global Business Dialogue in Washington D.C., 4 December 2003), online: <http://www.tradewinsllc.net/publi/Peace_Clause_GBD_12_03.pdf>

challengeable under the *SCM Agreement* provisions that could finally be applied after the peace clause expired?

Under a more superficial analysis, the simple answer would be “yes”: if the Peace Clause avoided the challengeability of agricultural subsidies under the *SCM Agreement* and this clause expired, then logically, these subsidies could be challenged under the *SCM Agreement*. However, the answer is not simple for several reasons.

First, the *SCM Agreement* procedural provisions to challenge subsidies were not conceived for agricultural products. In opposition, the *AoA* has substantive rules that specifically address agriculture, but its procedural provisions (Art. 13 and 19) do not provide a corresponding set of rules to regulate challengeability. Art. 19 only establishes that GATT Art. XXII and XXIII apply to consultations and disputes of the *AoA* and Art. 13, which is the goal of this research, actually restrains challengeability of *GATT 1994* and *SCM Agreement* to agricultural subsidies.

Second, even if the *SCM Agreement* procedural provisions automatically applied to the *AoA* substantive provisions, the legal boundaries of this challengeability are not very clear. Besides, the application is not automatic because of the high thresholds of challengeability of the *SCM Agreement*. As an example, there is doubt whether agricultural subsidies that comply with the *AoA* schedules (Annex II) can now be challenged under the *SCM Agreement* (Part II and specially Part III).

Third, the expiry is relatively recent, and it involves interpretation of the interrelationship among the three aforementioned WTO agreements as well as principles of international law,⁸

⁸ The ordinary meaning of various WTO texts applies principles of interpretation of international law. *Vienna Convention on the Law of the Treaties [The Vienna Convention]* Art. 32 Supplementary Means of Interpretation points out:

Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31: (a) leaves the meaning ambiguous or obscure; or (b) leads to a result which is manifestly absurd or unreasonable.

principles of the international trading system and GATT and WTO cases. Therefore, the answer is not static or flat because there is a new legal arrangement for the challengeability for agricultural subsidies whose regulation and recent cases are largely influencing and affecting each other in an interdependent and dynamic way, contributing to shape this new legal relationship. Recent WTO dispute settlement system decisions on agricultural subsidies are not developing hermetically.

If the answer is “no”, which would mean that the *SCM Agreement* provisions for challengeability cannot be used to challenge agricultural subsidies, then the expiry of the Peace Clause did not do much to improve the possibilities for challenging agricultural subsidies. And the first scholar to approach this question of challengeability stated that the answer was “no.” Didier Chambovey in his article⁹ published in 2002 titled “How the Expiry of the Peace Clause (Article 13 of the *WTO Agreement on Agriculture*) Might Alter Disciplines on Agricultural Subsidies in the WTO Framework,” established that there is conflict between the *AoA* and the *SCM Agreement*. The conclusion of this interpretation is that these Agreements cannot be applied together to regulate agricultural subsidies; therefore, the more specific must prevail according to the *lex specialis derogat legi generali* approach.¹⁰

The Vienna Convention on the Law of the Treaties, 23 May 1969, 1155 T.S. 331 (entered into force 27 January 1980). The *Vienna Convention* that gained the status of customary international law was internalized in the WTO system through the *Understanding on rules and Procedures Governing the Settlement of Disputes* [DSU] Art. 3.2 [WTO Legal Texts] at 354.; Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline* (1996) WTO Doc. WT/DS2/AB/R (Appellate Body Report), adopted 20 May 1996, as modified by Appellate Body Report WT/DS2/AB/R, DSR 1996:I, 29 [US – Gasoline]. See generally, David Palmeter and Petros C. Mavroidis, “The WTO Legal System: Sources of Law” (1998) 92(3) AJIL 398.

⁹ See Chambovey, Didier. “How the Expiry of the Peace Clause (Article 13 of the *WTO Agreement on Agriculture*) Might Alter Disciplines on Agricultural Subsidies in the WTO Framework” (2002) 36 *Journal of World Trade* 305 [Chambovey “Peace Clause”].

¹⁰ This principle establishes that in case of conflict, the most specific Agreement or provision prevails. Wilfred Jenks define the requirements that characterize the conflict:

“The *lex specialis derogat legi generali* principle ‘which [is] inseparably linked with the question of conflict’ between two treaties or between two provisions (one arguably being more specific than the other), does not apply if the two treaties ‘... deal with the same subject from different point of view or [is]

In this case, regarding the challengeability of agricultural subsidies, the *AoA* is the most specific; therefore, agricultural subsidies cannot be challenged under the *SCM Agreement*, which is the less specific. The consequence of this conclusion is that agricultural subsidization that has negative consequences, especially in poor countries, would continue without specific and clear limits of challengeability.¹¹

However in 2003, Richard Steinberg and Timothy Josling reached an opposite conclusion from that of Chambovey. They published an article¹² titled “When the Peace Ends: The Vulnerability of EC and US Agricultural Subsidies to WTO Legal Challenge” in which they stated that there was another way to resolve the problem of whether agricultural subsidies could be challenged under the *SCM Agreement*. They stated that the *GATT 1994*, *SCM Agreement* and *AoA*, according to the public international law principle of “effective interpretation,” had to apply cumulatively to create a coherent system to regulate agricultural subsidies. This principle states that these Agreements have to be interpreted together to give meaning and legal effect to all the terms.¹³ The consequence would be that agricultural subsidies could be challenged under the *SCM Agreement*, which would avoid a free-ride for agricultural subsidization.

Chambovey was right about his premise that the *SCM Agreement* and *AoA* could only be applied together if there were no conflict, but his conclusion that agricultural subsidies could not be challenged under the *SCM Agreement* because there was conflict was not accurate. Conversely, Steinberg and Josling reached a correct conclusion, but their premise was mistaken.

applicable in different circumstances, or one provision is more far-reaching than but not inconsistent with, those of the other” Wilfred Jenks, “The Conflict of Law-Making Treaties” (1953) 30 (BYIL) 425.

¹¹ The World Bank predicts that removing trade barriers in agriculture could take hundreds of millions of people out of poverty. There is an estimation that removal of trade barriers in agriculture by industrial countries could reduce poverty worldwide by 8%, or about 200 million people. William R. Cline, *Trade Policy and Global Policy*, (Washington, DC: Institute for International Economics, 2004) [Cline, *Trade Policy*].

¹² Steinberg, “Peace Clause” *supra* note 7.

¹³ This principle comes from the application of the *Vienna Convention* Art. 31 that states “[a] treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.” *The Vienna Convention supra* note 8.

The principle of “effective interpretation” gives general guidance on the interpretation of the WTO agreements, but the reason they can be applied together is because there is no conflict among them in regulating agricultural subsidies. If there were, the principle of “effective interpretation” would not avoid the application of the most specific agreement to resolve the conflict, which is the *AoA*. Therefore, even under the approach of Steinberg and Josling, agricultural subsidies could not be challengeable under the *SCM Agreement* because of their wrong premise.

This research aims to scrutinize and clarify the uncertainty in the interpretation and the application of the *AoA*, *SCM Agreement* and *GATT 1994* to challenge agricultural subsidies under the WTO. According to the main hypothesis of this study, after the expiry of the Peace Clause many agricultural subsidies can be legally challenged under the substantive provisions of the *GATT 1994* and the *SCM Agreement*, even if they comply with the limits established under the *AoA*. The new arrangement of the challengeability of agricultural subsidies after the expiry of the Peace Clause is being shaped not only by the interpretation and correlation of the aforementioned WTO agreements, but also by WTO cases. They play a relevant role in interpreting the rules and helping to define the new legal boundaries of agricultural subsidies.

In *United States – Upland Cotton*¹⁴ [*US – Upland Cotton*], the Appellate Body [AB] upheld the panel’s finding that determined that production flexibility, contract payments and direct payments were support measures that could be challengeable under *GATT 1994* Article XVI¹⁵ and Part III of the *SCM Agreement* by virtue of Article 13(a)(ii) of the *AoA*. This decision

¹⁴ Appellate Body Report, *United States – Subsidies on Upland Cotton* (2004) WTO Doc. WT/DS267/AB/R at para 763 (b) (i). (Appellate Body Report), adopted 21 March 2005, DSR 2005:I, 3 [*US – Upland Cotton*].

¹⁵ “Until the 1955 Review Section, Art. XVI consisted of only one paragraph containing simply a requirement that any contracting party that maintains a subsidy must notify GATT of the “extent ... nature ... estimated effect and ... circumstances of the subsidy and be prepared to consult as to possible injurious effects that it causes” John H. Jackson, *World Trade and the Law of GATT* (Charlottesville: The Michie Company Law Publishers, 1969) at 368 [Jackson, *Law of the GATT*]. Later, in 1955 in the Ninth Section of the Working Parties, Article XVI was amended

established that, even if agricultural subsidies complied with provisions and schedules of the *AoA*, they still could be condemned under the provisions of the *SCM Agreement* if they caused serious prejudice to another Member.

This study proves that there is no conflict among the *GATT 1994*, *SCM Agreement* and *AoA* regarding regulation of challengeability of agricultural subsidies. This conclusion is new because of the difficulties to determine the limits of application and overlapping of each of the three Agreements that regulate agricultural subsidies. First, this study analyzes general principles of international law, legal principles of interpretation and the relationship among the *AoA*, *SCM Agreement* and *GATT 1994* and panel and Appellate Body reports. It concludes that WTO provisions must be interpreted together.

In order to reach this conclusion, this study applies a two-pronged method to verify whether there was a conflict among WTO agreements that regulate agricultural subsidies: one theoretical and the empirical. These two methods were used because the examination of conflict must be based not only on jurisprudence and doctrine developed by scholars but also on decisions of international tribunals, especially the WTO.

Regulation of all types of agricultural subsidies in the *AoA*, *SCM Agreement* and *GATT 1994* were verified through these two methods, and no conflict was found, which means that the three Agreements can be applied together to regulate agricultural subsidies.

This examination also verifies that the thresholds of challengeability might have become higher after the implementation of the WTO, which might have contributed to make challengeability of agricultural subsidies more difficult. This study verifies through a

through the addition of Section B with paragraphs 2, 3, 4 and 5 that regulates exports subsidies. *GATT, Protocol Amending the Preamble and Parts II and III of the GATT*, Agreement No. 33 in App. C, 3d Supp. B.I.S.D. (1955) 222 at 224-27.

substantive¹⁶ analysis of GATT decisions that prior to the implementation of the WTO, there was condemnation of agricultural subsidies;¹⁷ which was not so common after the implementation of the *SCM Agreement* and the *AoA*¹⁸ for several reasons that will be demonstrated during this study. It might be an indication that market effect requirements for challengeability of agricultural subsidies brought by the *SCM Agreement* that were inherited from the Tokyo Round Subsidies Code¹⁹ [TRSC] increased the level of difficulty of the challenges.

This study does not make a comparative analysis of the efficiency of both the GATT and the WTO systems. Such analysis would require an evaluation of all provisions of the *GATT 1994*, all WTO agreements and a study of GATT and WTO cases not related only with agricultural subsidies. This research is limited to an examination of the limits of challengeability of agricultural subsidies in three moments of the international trading system's regulation.

Therefore, in a subsidiary way, the research demonstrates that, within these clear limits, the evolution from GATT to the WTO system²⁰ meant an increase in the complexity of the

¹⁶ Analysis of the substantive (subject matter) rules and the legal rationale of the cases concerning agricultural subsidization in contrast with procedural rules.

¹⁷ There were 21 cases of agricultural subsidies during the GATT years, which included disputes whose recommendations were not totally implemented. Out of these 21, 11 were satisfied and 10 were not satisfied, which means that there was no decision. This proves that 52.4% of the decisions satisfied the parties involved. Robert E. Hudec, *Enforcing International Trade Law: the Evolution of the Modern GATT Legal System* (Salem: Butterworth Legal Publishers, 1993) [Hudec, *Enforcing Trade Law*].

¹⁸ In several GATT cases analyzed in this study, agricultural subsidies were declared illegal under GATT Art. XVI, because they had given to the subsidizing country more than an equitable share of the world export trade in a specific product. *Ibid.* In other WTO cases, such as the *US – Upland Cotton supra* note 8 and Panel Report, *European Community – Export Subsidies on Sugar, Complaint by Australia* (2005), WTO Doc. WT/DS 265/R adopted 19 May 2005, as modified by Appellate Body Report WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, DSR 2005:XIII, 6499 [*EC – Export Subsidies on Sugar (Australia)*], the panels were not able to condemn agricultural subsidization under GATT Art. XVI.

¹⁹ The Code was negotiated under the auspices of the GATT Secretariat, but it was separate from the legal instruments existing side by side with the GATT. The TRSC was not signed by all GATT contracting parties and, for this reason, it was not a multilateral agreement. The following countries were the signatories of the Subsidies Code: Argentina, Australia, Austria, Brazil, Canada, Chile, Colombia, Egypt, the EC, Finland, Hong Kong, India, Indonesia, Israel, Japan, Korea, New Zealand, Norway, Pakistan, Philippines, Sweden, Switzerland, Turkey, United States and Uruguay. Olivier Long, *Law and Its Limitations in the GATT Multilateral Trade System* (Boston: Graham & Trotman, 1987) at 28.

²⁰ The word “system” is used here to describe substantive and procedural provisions and the cases decided during the GATT and WTO years.

provisions that regulate challengeability of agricultural subsidies because of the new provisions brought by the *SCM Agreement* inherited from the TRSC that reflected the fierce divergence of interests on agricultural policies between the two major forces in the GATT years: the US and the EC.

This is the reason the *SCM Agreement* does not automatically apply to all *AoA* provisions of subsidies after the expiration of the Peace Clause. There is no condemnation of agricultural subsidies *a priori*. It must be verified in a case-by-case basis if the challenged subsidy causes any type of adverse effect and if it complies with all the complex thresholds of challengeability of that specific adverse effect. Even a challenge under *SCM Agreement* Art. 3, which does not require proof of serious prejudice or injury to condemn export subsidization, has requirements for challengeability that must be fulfilled.

Taking into account that: a) the *GATT 1994* system had simpler rules and a rationale based on substantive rules that were not favorable to agricultural subsidization during the GATT years; b) the *SCM Agreement* was not originally conceived to define the boundaries of challengeability for agricultural subsidies; and, c) the *AoA* does not originally regulate challengeability; one possible solution to diminish the level of complexity was to establish simpler rules for challengeability of agricultural subsidies.

In order to address the basic questions outlined in the research's methodological problem, this dissertation covers specific periods of GATT and WTO history of agricultural subsidy legislation. As a result, it will analyze how the legal regime of agricultural subsidies, especially in regards to challengeability, has been shaped and modified during three important moments in international trade history: during the GATT years, during the WTO years before the expiry of the Peace Clause, and currently, after the expiry of the Peace Clause. A diagram presenting the

legal framework of challengeability for agricultural subsidies for that specific period of regulation will be presented at the conclusion of each part.

Part I of the dissertation will provide an analysis of the challengeability of agricultural subsidies before the Uruguay Round.²¹ This period of time is commonly known as the “GATT years,” when the WTO had not yet been established. Pertinent GATT provisions and cases will be examined to demonstrate the limits of challengeability during these years. The first part will also analyze the proposal of the TRSC during the negotiations of the Tokyo Round, including its implications for the current challengeability of agricultural subsidies and the transition between the Tokyo and the Uruguay Round.

Part II will study the challengeability of agricultural subsidies after the establishment of the WTO at the end of the Uruguay Round, on January 1, 1995, until the Peace Clause expired on December 31, 2003. This part of the dissertation will focus on the *AoA* and *SCM*, which shaped the boundaries of challengeability for agricultural subsidies before the expiry of the Peace Clause. It will include an analysis of the Agreement on Modalities, how they are calculated and the basic three pillars of agricultural regulation: market access, domestic support and export subsidies. This part will also include a study of the WTO’s *US – Upland Cotton* case. This dispute was the first case of WTO litigation on agricultural subsidies that faced the issue of the expiry of the Peace Clause. The relevance of this case and its impact on the interpretation of agricultural subsidies regulation the after Peace Clause expired will be demonstrated throughout the dissertation.

Part III will provide an analysis of challengeability of agricultural subsidies after the Uruguay Round and the application of a practical and a theoretical method to determine whether

²¹ The Uruguay Round (1986-1994) was used as a reference to divide the thesis because it created a new system of agricultural regulation with the set up of the *AoA* and *SCM Agreement*.

there is conflict among WTO agreements that regulate agricultural subsidies. The answer is that there is no conflict among them to regulate agricultural subsidies, and for this reason, they can be applied together.

The conclusion of the dissertation will have a diagram showing the comparative evolution of the legal boundaries of challengeability for agricultural subsidies during the GATT years, during the “peace period” and after the Peace Clause expired. It will assist in clarifying the current legal framework for challengeability applied to agricultural subsidies.

There are several works that explore the regulation of agricultural subsidies during the Uruguay Round. However, only a few articles have been written about the regulation of agricultural subsidies after the expiry of the Peace Clause. Economic and socially oriented volumes have explored the history of agricultural subsidies regulations, their social impacts in several countries and the political dimensions of farm subsidization.

As it is going to be seen throughout this research, agriculture also has one of the highest levels of trade distortions. It will be verified in the next chapter that while the share of agricultural exports from developing countries to developing countries has increased, their agricultural exports to developed countries diminished in the same period. Developing countries would benefit from liberalization, because, among other reasons, they would have more market access to developing and developed countries. Also, agricultural exporters (poorer countries) would benefit from higher agricultural prices.

Agriculture is significantly relevant for the economy of poor countries; however, it also has the highest levels of trade distortions, as is going to be demonstrated throughout this study. If WTO challenges to trade barriers on agriculture could have less complex and lower thresholds, perhaps these data would be different. The WTO was conceived to liberalize trade, however

agricultural subsidies remain at high levels and trade barriers continue to be imposed by developed countries against agricultural exports from developing countries.

Agricultural subsidies are the key point of the ongoing Doha Round, which is currently negotiating the future of the whole international trade system. Moreover, it is also the major point of disagreement stalling the negotiations. Most of the WTO Members are asking for agricultural subsidies reductions, whereas another group of Members is not willing to reduce their farming subsidies without market access concessions from other WTO Members.

Given the relevance of agricultural products for everyday life and the significance of the Doha Round for the future of international trade, it is time for a legal academic analysis of the problem. This dissertation seeks to contribute to legal academic literature to begin the work of filling this lacuna.

CHAPTER I

THE LEGAL SYSTEM OF AGRICULTURAL SUBSIDIES BEFORE THE URUGUAY ROUND

I.1 Background

Subsidies involve the direct transfer of funds, governmental revenue that is not collected or a governmental provision of goods and services other than general infrastructure and public payments.²² The problem is that agricultural subsidies can artificially shield recipients from market fluctuations and distort²³ the international prices for agricultural products.²⁴ This can constitute unfair trade, because it can undermine importing nations' WTO market access commitments²⁵ and displace exports from other WTO Members. For these reasons, agricultural subsidization violates fundamental principles²⁶ of the WTO.

Agricultural subsidies are a sensitive issue, because they have not only economic implications, but also cultural and political dimensions. Politically, farmers are important voters who have an efficient lobby in several countries. Culturally, they represent traditional values of the countryside and maintain cultural roots in several countries.

²² See *SCM Agreement* Art. 1.1 (a)(1)(i)(ii)(iii) and (iv). The concept of subsidy during the GATT years will be analyzed in section I.2.1.1, and the definition after the creation of the WTO will be analyzed in Part II of this research.

²³ The measurement of subsidies in the international trade field was studied by the OECD, which developed a set of measures for the purposes of comparing Member countries' levels of subsidies, types of subsidies and reductions under the *Uruguay Round Agreement on Agriculture*. The Aggregate Measurement of Support [AMS] is now used to estimate the dubbed "trade distorting" agricultural support measures, which are the support policies slated for reduction under the *AoA*. Timothy Wise. "The Paradox of Agricultural Subsidies: Measurement Issues, Agricultural Dumping, and Policy Reform" *Paper n. 04-02 from Global Development and Environmental Institute, 2004* (Medford: Tufts University, 2004).

²⁴ Cline, *Trade Policy supra* note 11 at 128 and 129.

²⁵ WTO market access conditions means the tariff and non-tariff measures agreed to by Members for the entry of specific goods into their markets. Each Member has a schedule of concessions with its tariff commitments.

²⁶ Trade without discrimination, free trade, predictability and promoting fair competition (http://www.wto.org/english/theWTO_e/whatis_e/tif_e/fact2_e.htm).

Since the First World War, agriculture has been subject to governmental regulation, mainly in Europe, assuring farmers certain guaranteed sales and protection against competition from imports from other countries. By the period of 1979–1981, the amount of money paid by OECD states to help their farmers reached 32% of their domestic agricultural prices on average. In the European Community it amounted to 43%, in the Scandinavian countries to 56%, and in Japan to 59%.²⁷ By 2004, the World Bank estimated that the level of agricultural subsidization was about one billion dollars a day²⁸. The International Monetary Fund [IMF] estimated that the costs of agricultural protection to taxpayers and consumers in the OECD countries alone amounted to about 300 billion dollars US each year,²⁹ and the amount was still growing in 2009–2010.³⁰

Alex F. MacCalla and John Nash state that agricultural trade needs reform for two basic main reasons “the importance of agriculture in developing countries and the slow growth of agricultural trade from developing countries to developed countries.”³¹

The authors state that agriculture is especially important for developing countries, because it remains the “largest employer, the largest source of GDP and the largest source of export and foreign exchange.” In developing countries, most of the citizens live in rural areas (75%). Their study shows that agriculture is significantly important for new economies, and it tends to decline when the economy of the country improves, which means that agriculture is

²⁷ International Food Policy Research Institute, Research Report 21, “Agricultural Protection in OECD Countries: Its Costs to Less Developed Countries” (December 1980) at 94.

²⁸ World Bank, *The World Development Report 2004: Making Services Work For Poor People* (Oxford: Oxford University Press, 2003).

²⁹ Trebilcock, Michael J. and Howse, Robert, *The Regulation of International Trade: Political Economy and Legal Order*. (London: Routledge, 1995) at 191 [Trebilcock, *The Regulation of Trade*].

³⁰ The OECD estimated that agricultural subsidies [producer support estimate –PSE] rose in 2010 to around 252.5 billion dollars or 22% of total farm receipts in 2009. This is more than the 21% share in 2008 and 22% in 2007. OECD, *Agricultural Policies in OECD Countries, at a Glance 2010* (Paris: OECD, 2010) at 5.

³¹ McCalla, Alex F. and Nash, John, eds., *Reforming Agricultural Trade for Developing Countries, Key Issues for a Pro-Development Outcome of the Doha Round*, Volume I (Washington, DC: The World Bank, 2007) at 2 [McCalla, “Reforming Agricultural Trade”].

more important for countries at the “early stages of development,” as the table below clearly demonstrates.³²

Table 1: Rural-Urban Poverty Gap

Poverty Rates	Burkina	Mauritania	Mozambique	Zambia	Gambia	Cambodia	Kyrgyzstan	Nicaragua
Rural	51	68	71	80	61	40	70	69
Urban	17	25	62	56	48	21	49	31
Dif.	34	43	9	24	13	19	21	38

Agriculture is significantly relevant for poor countries; however, it also has the highest levels of trade distortions, as is going to be demonstrated throughout this study. Therefore, perhaps reform to make the challengeability of agricultural subsidies simpler would help poor countries that depend on agriculture to provide wealth to their citizens.

Other important data show that, even though trade rates have peaked during the last decades, there is a slight growth in agricultural trade from developing to developed countries. This data is even more significant if we note that the trade of developing countries is consistently growing. Manufactured exports from developing countries to developing and developed countries are booming, but agricultural exports from developing countries vary in quantity. They are increasing at greater rates to developing countries than to developed countries. “The share of developing countries in agricultural exports to the industrial world has stagnated,” as the table³³ below demonstrates.

³² Originally, the table had twenty-one countries. Eight were used as an example. The 13 that did not fit in this illustrative table were Uganda (46, 16, 30), Tanzania (50,24, 26), Niger (66, 52, 14), Ethiopia (47, 37, 10), Ghana (34, 27, 7), Malawi (67, 55, 12), Vietnam (57, 26, 31), Mongolia (33, 39 – 6), Georgia (10, 12, - 2), Honduras (51, 57, -6), Yemen (45, 31, 14), Nepal (44, 23,21), Sri Lanka (27, 15, 12). The first number in the columns refers to rural, the second to urban and the third is the difference between the two. The source was the Calculations from Poverty Reducing Strategy Papers for Each Country in *Ibid* at 2.

³³ The source was the United Nations Statistics Division, Comtrade Database in *Ibid.* at 3.

Table 2: Share of Developing Countries' Exports in World Trade

	1980/1981	1990/1991	2000/2001
Total Agricultural Exports	35.4	32.2	36.3
To Developing Countries	9.5	8.9	13.4
To Industrial Countries	25.8	23.3	22.9
Total Manufacturing Exports	19.3	22.7	33.4
To Developing Countries	6.6	7.5	12.3
To Industrial Countries	12.7	15.2	21.1

While the share of agricultural exports from developing countries to developing countries increased from 9.5% to 13.4%, their agricultural exports to developed countries diminished from 25.8% to 22.9% in the same period. A causal link cannot be proved, but the data indicate that trade barriers imposed by developed countries to agricultural imports from developing countries might have made such exports more difficult. If WTO challenges to trade barriers on agriculture could have less complex, lower thresholds, perhaps these data would not be the same.

One of the main goals of the international trading system is trade liberalization. If agricultural subsidies remain at such a high level and trade barriers are easily being imposed by developed countries against agricultural exports from developing countries, this goal has not been yet accomplished for agriculture.

According to the WTO, trade liberalization brings development.³⁴ The whole system was conceived because of this concept. Since the GATT years, the goal of the rounds was to diminish tariffs and to eliminate trade barriers. It is estimated that developing countries would raise their incomes by 0.8 % more by 2015 if agricultural subsidies and trade barriers were removed

³⁴ See Ingco, M. and J. Nash. *Agriculture and the WTO: Creating a Trading System for Development* (Washington, DC: Oxford University Press and the World Bank, 2004).

between 2005 and 2010, and two-thirds of this gain would come from subsidy reform and agricultural trade.³⁵

Some scholars state that developing countries would benefit from liberalization, because they would have more market access to developing and developed countries. Also, agricultural exporters (where poverty is concentrated) benefit from higher agricultural prices. Studies say that liberalization would raise net farm incomes in Africa by an average of 7%, and the result would be that 32 million people would be out of poverty, most in Sub-Saharan Africa.³⁶

Some scholars³⁷ have stated that net food importers in particular, such as some African poor countries, might have financial problems when prices of agricultural products rise, which is already happening. However, Tangermann states that liberalization would even improve the GDP of net food importers.³⁸ There is an estimation that these countries, especially least developed countries (LDC) could have a total of income losses around US\$ 200.00 to US\$ 300.00 million, which does not jeopardize liberalization but has to be considered by the international community.³⁹ In general, studies show that the positive consequences of trade liberalization offset possible negative impacts.⁴⁰

Finally it is relevant to state that this thesis will exclusively examine the legal structure for the challengeability for agricultural subsidies, which precludes an examination of other aspects of agricultural subsidization. The dissertation limits its scope in four ways. Firstly, the legal framework of non-agricultural subsidies, such as industrial or fisheries, which have a

³⁵ Anderson, K., W. Martin, and D. van der Mensbrugge, "Would Multilateral Trade Reforms Benefit Sub-Saharan Africans?" (2006) 15 *Journal of African Economies* 626 at 7 [Anderson, "Trade Reforms and Africa"].

³⁶ See McCalla, "Reforming Agricultural Trade" *supra* note 31 at 4.

³⁷ Cline, *Trade Policy* *supra* note 11.

³⁸ Tangermann, Stefan, "Organization for Economic Cooperation and Development Area Policies and the Interests of Developing Countries" (2005) 87(5) *American Journal of Agricultural Economics* 1128.

³⁹ Hoekman, B., W. Martin, and C. A. P. Braga, "Preference Erosion: The Terms of the Debate." In Newfarmer, R. ed., *Trade, Doha, and Development: A Window Into the Issues*, (Washington DC: World Bank, 2005).

⁴⁰ Anderson, "Trade Reforms and Africa" *supra* note 35.

specific regulation, is beyond the scope of this study. Secondly, WTO regulation is the focus of analysis of this study, which means that no other international or national legislation on agricultural subsidies will be studied. The third limitation is that the dissertation does not investigate economic and social aspects of agricultural subsidies in depth. It only discusses the aspects of some of these factors that might have influenced the GATT and the WTO and their decisions.

Therefore, non-legal issues related to agricultural subsidies, such as the social disparities created by the use of agricultural subsidies or the economic consequences surrounding it, are beyond the scope of this study. This does not mean that this dissertation will not occasionally mention some social, economic or even political and cultural aspects of agricultural subsidies; they can be relevant to explaining particular legal aspects of this study.

The last limitation is that the dissertation does not exhaustively analyze all aspects of the legal framework for agricultural subsidies. It focuses on the analysis of *GATT 1994* provisions for subsidies, *SCM Agreement* articles that regulate challengeability and *AoA* Article 13 (the Peace Clause) and other articles on subsidies in the Agreement. Other aspects of the regulation are also beyond the scope of this study.

I.1.1 Agricultural Subsidies in the *GATT 1947*

This thesis seeks to define the current legal regime for the challengeability for agricultural subsidies. The first part of the research analyzes the challengeability of agricultural subsidies under the GATT system (the first of the three moments of regulation of the international trading system analyzed in this study). The goal is to clearly define the limits of

challengeability prior to the Peace Clause in order to compare with the other moments analyzed in this study. It helps to elucidate the evolution of the provisions and the requirements needed for challengeability. This analysis demonstrates that, despite the GATT's less sophisticated legal system if compared with the WTO system, GATT decisions had a rationale that made condemnation of this sort of subsidization possible.

The thesis will demonstrate that during the GATT years, agricultural domestic and export subsidies could be challenged under *GATT 1947* Arts. XVI, VI, and XXIII through Arts. II and III. For this purpose, the articles that shaped the regulation of the challengeability of agricultural subsidies and some GATT cases that helped to outline the legal boundaries of such regulation will be analyzed. To this end, it is necessary to first delineate the reasons why subsidies are such a controversial issue that has stalled Doha Round negotiations and also to clearly define the limits of this research.

Lastly, this first part of the dissertation is divided into six sections. The first presents the introduction to domestic subsidies and defines the limits of this research. The second analyzes the legal structure and challengeability of *GATT 1947* Art. XVI, which represented the main possibility for challengeability of agricultural subsidies during the GATT years. This part also studies the Havana Charter, which was relevant for the legal structure of Art. XVI and also some GATT cases that condemned agricultural subsidization under Art. XVI. The third scrutinizes the Tokyo Round, which brought about a new code on subsidies and changes in procedural legislation for agricultural subsidies. It also analyzes some GATT cases that were brought under the Tokyo Round Subsidies Code and verifies that they failed to condemn agricultural subsidization under the new provisions. The fourth part examines other possibilities of challengeability of agricultural subsidies during the GATT years: Art. VI, II and III through

XXIII 1(b) and their respective cases. The fifth section evaluates the balance of power during the GATT years and the consequent US waiver, and the sixth presents the conclusions of this first part of the dissertation.

I.1.2 The GATT Legal Framework for the Challengeability of Agricultural Subsidies

The regulation of agriculture in international trade began in 1947 with the approval of the *GATT 1947*. The Agreement shaped the legal disciplines for international trade and set up general rules for subsidies in Art. XVI. Other articles applied to agricultural products as well, such as Arts. II, III and XI, but Art. XVI established the regime for subsidies.

The fact that agriculture was included in the *GATT 1947* was a considerable accomplishment for contracting parties⁴¹ who defended trade liberalization. According to Hudec, during the GATT years, perhaps because of the political influence of the European countries, there was an acceptance – or resignation – that agricultural trade should be less regulated than non-agricultural trade. At that point, the European countries were concerned that, in order to include agricultural products in the GATT agenda of liberalization, the highly complex agricultural policies and regulations of the European countries had to be changed.⁴²

Despite all the difficulties in including agriculture in the *GATT 1947* agenda, all of the 38 *GATT 1947* articles were equally applicable to industrial and agricultural goods, which was a significant victory for trade liberalization in agriculture. There was a special article that applied

⁴¹ Explanatory Note 2 (a) of *GATT 1994* states that “[t]he reference to ‘contracting party’ in the provision of *GATT 1994* shall be deemed to read ‘Member.’” This research will use the word “contracting party” to refer to GATT Members prior to 1994, and “Member” to refer to GATT Members after this date.

⁴² “The EC’s Common Agricultural Policy (CAP) soon provided a clear test for *GATT 1947*’s weakened regulatory framework. As the blueprint unfolded, it became clear that the EEC was claiming the right to almost complete autonomy over agricultural trade policy.” Hudec, Robert E., *The GATT 1947 Legal System and the World Trade Diplomacy*, 2d. ed. (New York: Butterworth Legal Publishers, 1990) at 216 [Hudec, *World Diplomacy*].

only to subsidies that shaped the *GATT 1947* regulation for agricultural subsidies: Article XVI.⁴³ *GATT 1947* Article XVI⁴⁴ set the foundation for subsidy regulation (both agricultural and non-agricultural) before the creation of the WTO.⁴⁵

I.2 Subsidies under *GATT 1947* Article XVI

GATT 1947 Article XVI regulated the legal system on subsidies until the creation of the WTO in 1995. Section A regulated domestic subsidies in general (agricultural and non-agricultural), whereas Section B, which was added in 1955,⁴⁶ set rules for export subsidies. Section A established that any contracting party that gave subsidies, “including any form of income or price support,” that directly or indirectly increased exports or reduced imports “shall notify in writing the contracting parties” about their quality and quantity and the reasons for subsidization.

⁴³ “*GATT 1947* Art. XVI:

Subsidies ... Section B Additional Provisions on Export Subsidies ... 3 Accordingly, contracting parties should seek to avoid the use of subsidies on the export of primary products. If, however, a contracting party grants directly or indirectly any form of subsidy which operates to increase the export of any primary product from its territory, such subsidy shall not be applied in a manner which results in that contracting party having more than an equitable share of world export trade in that product, account being taken of the shares of the contracting parties in such trade in the product during a previous representative period, and any special factors which may have affected or may be affecting such trade in the product.

⁴⁴ *GATT 1947* Art. III, XI and VI also are subsidies-related but do not regulate them directly. Art. III regulates national treatment on internal taxation, Art. XI, general elimination of quantitative restrictions and Art. VI, antidumping and countervailing duties.

⁴⁵ However, in 1890, the US adopted a countervailing duty law that was extended in 1922 to cover domestic subsidies. It was originally applied only to exports that were dutiable in the US. Canada, in contrast, was the first country, in 1904, to regulate the imposition of anti-dumping duties in cases where the export price of imported merchandise was lower than its fair market value in the exporting country in . J. F. Beseler, & A. N. Williams, *Anti-Dumping and Anti-Subsidy Law The European Communities*. (London: Sweet & Maxwell, 1986) at 3-4.

⁴⁶ See *supra* note 15.

I.2.1 Domestic Subsidies and the Concept of “Subsidy” and “Serious Prejudice”

The *GATT 1947* did not have a precise definition of subsidy. The description of subsidy in the first part of *GATT 1947* Art. XVI was “any form of income or price support, which operates directly or indirectly to increase exports of any product from, or to reduce imports of any product into, its territory.”⁴⁷ If a contracting party subsidized a product that had any impact on the imports or exports of any other contracting party, other contracting parties had to be notified of this subsidy. The subsidizing country had to explain the nature of the subsidization, estimate its effects and explain why the subsidies were used.

GATT 1947 Art. XVI only stated that the definition included any form of income or price support. The meaning of words such as “income” or “price support” was not defined. In 1961, a “Panel on Subsidies” was established to conduct a “Report on the Operation of the Provisions of Article XVI” with the goal of evaluating the application of this provision, and some conclusions were reached. The Panel, in paragraph 23, decided that “it was neither necessary nor feasible to seek an agreed interpretation of what constituted a subsidy. It would probably be impossible to arrive at a definition which would at the same time include all measures that fall within the intended meaning of the term in Article XVI.” The panel declared, however, that “the lack of a precise definition had not, in practice, interfered with the operation of Article XVI.”⁴⁸

Besides, there had been clarification about the concept of subsidies in a previous report, in which the panel discussed the circumstances where a system of domestic fixed prices above the world level might be considered a subsidy in the meaning of *GATT 1947* Art. XVI. It reached the conclusion that a system that used direct and indirect methods to maintain such a price

⁴⁷ See *GATT 1947* Art. XVI 1.

⁴⁸ *GATT, Panel on Subsidies, Report on the Operation of the Provisions of Article XVI*, *GATT* Doc. L 1.442 (1961), online: WTO <<http://docsonline.wto.org/gen. search/asp>> at 8.

through purchases or resale at a loss could also be a subsidy. Holding stocks could be considered one of the methods to maintain the price. The panel established exceptions to this rule and also recognized that other variations of price stabilization could characterize a subsidy, which should be analyzed by an examination of each case.⁴⁹

The panel also examined the question of whether non-governmental financial assistance could be considered a form of subsidy under the *GATT 1947*. The answer was that the concept of a subsidy was necessarily linked with governmental assistance in any form. *GATT 1947* was not concerned with actions taken by private persons acting independently of their governments; therefore, the panel recommended that contracting parties should ask their governments to “notify all levy/subsidy schemes affecting imports or export which are dependent for their enforcement on some form of government action.”⁵⁰

Some criteria for a determination of the existence of a subsidy were defined in the Committee on Trade in Agriculture. In its meeting on November 30, 1983, this Committee prepared a report, an examination of the operation of the *GATT 1947* regarding domestic, export and other subsidies. The report discussed the following definition of subsidy: “a transfer of government resources to a specific area of economic activity in a way which may be discriminatory to alternative potential domestic recipients of this type of transfer.”⁵¹ Even though GATT contracting parties acknowledged that a lack of definition of a subsidy was not a problem,⁵² an effort to define what a subsidy was during the GATT years was realized from 1980 onwards, as the report shows.

⁴⁹ *GATT, Panel on Subsidies and State Trading, Report on Subsidies*, GATT Doc. L 1.160 (1960), online: WTO <http://docsonline.wto.org/gen_search/asp> at para. 11.

⁵⁰ *Ibid.* at para. 12.

⁵¹ *GATT, Draft Report of the Committee on Trade in Agriculture, Note by the Secretariat*, GATT Doc. AoA/W/5 (1984), online: WTO <http://docsonline.wto.org/gen_search/asp> at para. 48 [*GATT CTA Report*].

⁵² See *supra* note 41.

Through this definition and the reports analyzed above, it can be concluded that the concept of “subsidy” during the GATT years was linked with governmental assistance to an area of economic activity – which excludes subsidies designed to benefit one specific user –and “discrimination” against alternative potential domestic recipients of the transfer. Actually, it can be verified that this definition had all the basic concepts of the *SCM Agreement* definition in Art. 1, which came later during the WTO years: use of resources, the government as the agent and discrimination. The term “discrimination” here means a benefit that could be given to several potential recipients but is only given to some of them. The concept in *SCM Agreement* Art. 1 will be analyzed in depth further in this study.

Regarding the term “benefit,” the GATT Committee of Subsidies and Countervailing Measures agreed that the concept of a subsidy had to include not only a charge on the public account, but also a benefit that had to be given to an industry.⁵³

GATT 1947 Art. XVI, second sentence, stated that a possible limitation to subsidization should take place if it caused serious prejudice, which means that the *GATT 1947* created a system that made it possible for contracting parties to challenge domestic subsidization that had caused serious prejudice. Therefore, it is necessary to define the concept of “serious prejudice” during the GATT years. This concept was fundamental for the challengeability of agricultural subsidies and changed over the years after the implementation of the *AoA* and the *SCM Agreement*.

There was no clear definition of “serious prejudice” in the *GATT 1947*. We can conclude by the reading of the second sentence of *GATT 1947* Art. XVI that, in order to cause serious prejudice, a subsidy had to at least have an impact on the imports or exports of the subsidizing

⁵³ *GATT 1947, EEC Memorandum in US Final Countervailing Duties Determinations on European Steel Exports, Committee on Subsidies and Countervailing Measures, GATT Doc. SCM Agreement/35 (1982)*, online: WTO <<http://docsonline.wto.org/gen. search/asp>> at 4.

country. Therefore, the concept of serious prejudice in the *GATT 1947* was linked with an alteration of imports or exports of the product involved. There was no market-effect requirement to characterize serious prejudice in the *GATT 1947*.

Several⁵⁴ disputes mentioned the concept of serious prejudice, but only two analyzed the concept under the *GATT 1947*:⁵⁵ *European Community – Refunds on Exports of Sugar – complaint by Australia [EC – Sugar Exports (Australia)]*⁵⁶ and *European Communities – Refunds on Exports of Sugar – Complaint by Brazil [EC – Sugar Exports (Brazil)]*.⁵⁷ In *EC – Sugar Exports (Australia)*, the panel held that the Community refunds on sugar exports had contributed to depressing world sugar prices, and for this reason, serious prejudice had been caused to Australia. This was the first time that the concept of serious prejudice was linked to a market effect factor – price depression. The panel also held that, because export refunds for sugar had no effective limitations either on production, price or the amount of export refunds, they constituted prejudice within the definition of Article XVI:1.⁵⁸

In *EC – Sugar Exports (Brazil)*, the panel concluded that the quantity of sugar made available for export by the Community and the non-limited subsidies that financed export

⁵⁴ *GATT 1947 Panel Report, European Economic Community – Subsidies on Export of Wheat Flour, SCM Agreement/42*, 21 March 1983, unadopted [*EEC – Wheat Flour Subsidies*], *GATT 1947 Panel Report, European Community – Refunds on Exports of Sugar*, L/4833, adopted 6 November 1979, BISD 26S/290 [*EC – Sugar Exports (Australia)*], *GATT Panel Report, European Community – Refunds on Exports of Sugar – Complaint by Brazil*, L/5011, adopted 10 November 1980, BISD 27S/69 [*EC – Sugar Exports (Brazil)*], *GATT Panel Report, EEC – Import Regime for Bananas*, DS38/R, 11 February 1994, unadopted [*EEC – Bananas II*], *GATT Panel Report, Panel on United States – Measures Affecting Imports of Softwood Lumber from Canada, SCM Agreement/162*, adopted 27 October 1993, BISD 40S/358 [*US – Softwood Lumber II*], *GATT Panel Report, Imposition of Countervailing Duties on Imports of Fresh and Chilled Atlantic Salmon from Norway, SCM Agreement/153*, adopted 28 April 1994, BISD 41S/576 [*US – Norwegian Salmon CVD*], *GATT Panel Report, European Economic Community – Payments and Subsidies Paid to Processors and Producers of Oilseeds and Related Animal-Feed Proteins*, L/6627, adopted 25 January 1990, BISD 37S/86 [*EEC – Oilseeds I*], *GATT Panel Report, EEC – Member States' Import Regimes for Bananas*, DS32/R, 3 June 1993, unadopted [*EEC – (Member States) Bananas I*] and *GATT Panel Report, German Exchange Rate Scheme for Deutsche Airbus, SCM Agreement/142*, 4 March 1992, unadopted [*EEC – Airbus*].

⁵⁵ The other cases analyzed the concept under the Tokyo Round Subsidies Code's provisions.

⁵⁶ *EC – Sugar Exports (Australia)* *supra* note 54.

⁵⁷ *EC – Sugar Exports (Brazil)* *supra* note 54.

⁵⁸ *EC – Sugar Exports (Australia)* *supra* note 54 at paras. (g) and (h).

refunds contributed to depressing sugar prices, and that constituted a serious prejudice to Brazilian interests according to the *GATT 1947* Art. XVI. The panel also held that the Community had not worked to limit its subsidies either on production or price. Therefore, this constituted a permanent source of uncertainty in the world sugar market and, for this reason, represented a threat of serious prejudice within the meaning of Article XVI:1.⁵⁹

The panels based their determination of serious prejudice on the fact that the Community did not limit export refunds and was continually subsidizing, which brought instability to the international sugar market and ultimately affected the quantity of production and the price. It is important to note that *GATT 1947* Art. XVI did not establish a clear link between serious prejudice and market-effect factors such as price and production. These market-effect factors were part of the equation to prove serious prejudice but not a formal requirement, without which challengeability would not be possible.⁶⁰

In conclusion, during the *GATT 1947* years, adverse effect could be found if a subsidy operated in a way as to increase exports or reduce imports. There was no market-effect requirement in the *GATT 1947* to challenge subsidies under the allegation of adverse effect, such as decline in output, sales, market share, profits and other economic factors later introduced by the Tokyo Round Subsidies Code [TRSC] and by the *SCM Agreement*.

⁵⁹ *EC – Sugar Exports (Brazil) supra* note 54 at paras. (f) and (g).

⁶⁰ Even though, there was not a clear concept of serious prejudice in the *GATT 1947*, the requirements for its determination were evolving over the years from a subjective evaluation to a more practical assessment. “[E]lements of fact and not subjectivity should be present in the determination of prejudice. One view was that the discussion could be engaged only if it were determined that a subsidy caused or threatened to cause prejudice, and not if it were just felt that a subsidy could cause prejudice.” *GATT CTA Report supra* note 51 at 58.

I.2.2 Export Subsidies and the Concept of “More Than an Equitable Share of the World Export Trade”

It is relevant to note that, until 1955, *GATT 1947* Art. XVI had only the first paragraph, Section A, analyzed above. During the Ninth Review Section, several provisions of the *GATT 1947* were reviewed and section B was added, including four paragraphs that regulated export subsidies.⁶¹ This section clearly determined that contracting parties recognized that export subsidization might cause harmful effects and undue disturbance and that it might hinder the achievement of the GATT goals.

Paragraph 3 of section B suggested that *GATT 1947* Members avoid export subsidies of agricultural products. The paragraph imposed a limit for agricultural export subsidization. It stated that export subsidies engaged in by any contracting party could not give more than an “equitable share of the world export trade in that product.”⁶² This expression was criticized as not being accurate in defining in which circumstances agricultural export subsidization should be limited.

Several *GATT 1947* cases⁶³ scrutinized the “equitable share” concept and condemned agricultural subsidies under *GATT 1947* Art. XVI. This proved that, even though *GATT 1947* rules did not always have very detailed terms, they were effective in limiting agricultural subsidization that caused harmful effects to any contracting party.

⁶¹ John Jackson explains the history of the Review Section that added four paragraphs on export subsidies on *GATT 1947*:

With several years it became apparent to *GATT* representatives and leaders that it would be necessary to take an overall look at *GATT* and to revise it in the hope that it could more adequately fulfill the role into which it had reluctantly fallen. The Ninth Section of the Contracting Parties of *GATT*, held from October 28, 1954 to March 18, 1955, was to be the “Review Section” during which the entire *GATT* treaty would be examined and restructured. At this section a large number of proposals were received for changing various provisions of *GATT*, many of which reflected the changes that had been made in the ITO Charter at the Havana Conference but which had not been heretofore brought into the *GATT* itself. Jackson, *Law of GATT supra* note 15 at 51.

⁶² See *GATT 1947*, Article XVI, Section 3.3.

⁶³ Hudec, *Enforcing Trade Law supra* note 17.

Paragraph 4 established that any form of non-agricultural export subsidization should be ceased if the subsidies resulted in the sale of the product for export at a price lower than that applied in the domestic market for a like product. These barriers were the base for all the later prohibitions and limitations of domestic and export subsidies found in the *AoA* and the *SCM Agreement*.

Paragraph 4 also exempted primary⁶⁴ goods from its general prohibition on export subsidies. This exception⁶⁵ for agricultural products helped to shape the legal boundaries of agricultural subsidies. However, agricultural export subsidies were allowed only if they did not give the subsidizing country “more than an equitable share of the world export trade in that product.”⁶⁶

The wording of the current *GATT 1994* regulation on challengeability of subsidies, especially for export subsidies originated in the Havana Charter. Therefore, in order to study the meaning of “more than an equitable share in the world export trade” in *GATT 1947* Art. XVI, it is necessary to make a historical analysis of the Charter and compare its provisions for export subsidies to *GATT 1947* Article XVI.

⁶⁴ Interpretative Note Ad 2 of Section B of *GATT* Article XVI in Annex I defines a primary product as “any product of farm, forest or fishery, or any mineral, in its natural form or which has undergone such processing as is customarily required to prepare it for marketing in substantial volume in international trade.” The definition comes from Article 56.1 of the 1948 Havana Charter, which refers to primary products as “a group of commodities, of which one is a primary commodity as defined in paragraph 1 and the others are commodities, which are so closed related, as regards conditions of production or utilization, to the other commodities in the group, that it is appropriate to deal with them in a single Agreement.” The definition is a clear reference to agricultural products as defined in *France – Assistance to Exports of Wheat and Wheat Flour L/924*, adopted 21 November 1958, BISD 7S/46 [*France – Wheat Exports*] and *EEC – Wheat Flour Subsidies supra* note 47. For this reason agricultural and primary products will be used in this study in the same sense.

⁶⁵ “Further, efforts to address subsidies more directly led to extensive amendments of Article XVI in 1955, prohibiting export subsidies on non-primary products and setting out trade effects concepts in an attempt to limit the use of subsidies on the export of primary products. In 1960, further elaboration was provided through an illustrative list of export subsidies.” Williams, Terry. & Salembier, Gerry. “International Disciplines on Subsidies: the GATT, the WTO and the Future Agenda” (1996) 30 *The Journal of World Trade* 5 at 5.

⁶⁶ See *GATT 1947* Art. XVI:3.

I.2.2.1 The Havana Charter

In 1947, the International Trade Organization [ITO] was being negotiated, with a supposedly more stringent regulation for subsidies. However, the ITO never came into existence, because the US decided not to submit the ITO to the US Congress for approval. Therefore, the *GATT 1947* had to be reformed to accommodate new provisions that were in the Havana Charter and that had been supposed to have been implemented through the ITO. The first paragraph of *GATT 1947* Art. XVI had the same wording as Art. 25 of the Charter.⁶⁷

The *GATT 1947* was not meant to be a complete system or an organization, but an international contract with limited purposes. Nevertheless, because the ITO never came into existence, the *GATT 1947* became an Agreement that was somewhat different from what it was originally conceived to be and had to fill some gaps created by the ITO's failure.⁶⁸ The main goal of the *GATT 1947*, according to the purposes of trade liberalization, was to protect tariff concessions among contracting parties. *GATT 1947* Art. XXIX established that the contracting parties should comply with the provisions of Part II of the *GATT 1947*, which would have been

⁶⁷ The Havana Charter Art. 25 Subsidies in General:

If any Member grants or maintains any subsidy, including any form of income or price support, which operates directly or indirectly to maintain or increase exports of any product from, or to reduce, or prevent an increase in, imports of any product into, its territory, the Member shall notify the Organization in writing of the extent and nature of the subsidization, of the estimated effect of the subsidization on the quantity of the affected product or products imported into or exported from its territory and of the circumstances making the subsidization necessary. In any case in which a Member considers that serious prejudice to its interests is caused or threatened by any such subsidization, the Member granting the subsidy shall, upon request, discuss with the other Member or Members concerned, or with the Organization, the possibility of limiting the subsidization.

UN, Final Act and Related Documents of United Nations Conference on Trade and Employment held at Havana, Cuba, *Havana Charter for an International Trade Organization* (April, 1948), online: WTO <http://www.wto.org/english/docs_e/legal_e/havana_e.pdf> [*The Havana Charter*].

⁶⁸ Jackson states that the GATT was not an "organization" but a mere international contract "with limited purposes." In his opinion, "subsequent developments of GATT, particularly its movement to fill the vacuum left when the ITO failed, have pushed GATT into a broader role than was initially conceived for it." John Jackson, *World Trade and The Law of GATT*, (Virginia: Law Publisers, 1969) at 49 [Jackson, *Law of GATT*].

suspended if the Havana Charter had come into force. Also, no provision of the *GATT 1947* should be invoked if it would prevent the operation of any provision of the Charter.⁶⁹

GATT 1947 Art. XXIX showed that some provisions of the Agreement were originally meant to be temporary. Paragraph 4 of Article XXIX established that, if the Havana Charter ceased to be in force, the contracting parties would meet as soon as possible to supplement, amend or maintain the provisions of the *GATT 1947*.

Art. 26 of the Havana Charter also had four paragraphs on additional provisions on export subsidies that were used as the base for section B of the *GATT 1947*. The first paragraph established that no Member should grant subsidies that would result in the export of a product at a lower price than a like product in the domestic market. This provision was similar to the one established under *GATT 1947* Art. XVI, paragraph 4, but it did not exempt agricultural products from its general prohibition of export subsidies. Agricultural products were treated in Arts. 27 and 28 of the Havana Charter.

It is relevant to observe that the prohibition of export subsidization either in the *GATT 1947* or in the Havana Charter was linked to the condition that the subsidy had to result in the sale of the product in question for export at a price lower than the comparable price charged for a like product in the domestic market.

It was less difficult to prove that the export subsidy had given to the Member more than an “equitable share of the world export trade” in one specific product than to prove that the subsidy had caused the subsidized product to be sold at a price lower than that for a comparable one in the domestic market. The requirement of *GATT 1947* Art. XVI:4 involved not only market-effect evaluations on exports, but also in the domestic market. This is one of the main reasons that most of the *GATT 1947* cases on export subsidies challenged the “equitable share”

⁶⁹ See *GATT 1947* Art. XXIX paragraphs 1, 2 and 6.

provision and not the exception linked to the prohibition of export subsidization stated in *GATT 1947* Art. XVI, paragraph 4.

The second paragraph of Art. 26 of the Charter established that an exemption for duties on export products should not be considered as a subsidy. Paragraph 3 determined that a maximum deadline of two years should be awarded for the accomplishment of what was established in paragraph 1. Paragraph 4 allowed export subsidization to offset a given subsidy that affected the export of that product. Even though Art. 26 of the Havana Charter limited the use of subsidies, it was not as explicit as *GATT 1947* section B in determining that export subsidies had harmful effects.⁷⁰

Paragraph 2 of *GATT 1947* Art. XVI clearly stated that export subsidies could cause harmful effects and undue disturbance to *GATT 1947* contracting parties and could hinder the achievement of the objectives of the *GATT 1947*. In this aspect, the *GATT 1947* was more explicit in limiting export subsidies and in consequently reaching the objectives of trade liberalization established by the international trading system.

As was stated, Arts. 27 and 28 of the Havana Charter exclusively regulated agricultural subsidies. Art. 27 prescribed two specific circumstances under which agricultural subsidies could not be prohibited under Art. 26.1 (prohibition of a subsidy that resulted in exports at a lower price than that for a like product in the domestic market). The first circumstance arose if the subsidy also resulted in the sale of the product at a higher price than a like product would have obtained in the domestic market; the second, if the subsidy did not cause serious prejudice to other Members.⁷¹ These two conditions were already in *GATT 1947* Art. XVI. The Havana

⁷⁰ See *GATT 1947* Art. XVI:2.

⁷¹ The Havana Charter Art. 27 *Special Treatment of Primary Commodities*. 1. A system of the stabilization of the domestic price or of the return to domestic producers of a primary commodity, independently of the movements of export prices, which results at times in the sale of the commodity for export at a price lower than the comparable

Charter did not exempt agricultural products from the general prohibition on export subsidies found in Art. 26 but, nonetheless, found a way to make rules less stringent for agricultural subsidies than for subsidies in general.

Paragraph 2 of Art. 27 established that any Member that gave agricultural subsidies could establish “Inter-Governmental Commodity Agreements,” according to Chapter VI of the Havana Charter. This chapter stated that agricultural subsidization might create special difficulties, which might have serious adverse effects on the interests of producers and consumers, “jeopardizing the general policy of economic expansion.”⁷² It also recognized that agricultural products deserved special treatment.

The goals of these Agreements were to prevent economic difficulties when adjustments between production and consumption could not be made by normal market forces, develop agricultural product industries, prevent fluctuations in the price of agricultural products, prevent exhaustion of natural resources, provide expansion of agricultural production and guarantee equitable distribution of agricultural products in short supply.⁷³ The main purpose was to control agricultural production and even prices⁷⁴ through a system of surveillance of commodities that could be requested by any Member. The system had specific procedures for dispute settlement through the Commodity Council and established rules for the commodity agreements that aimed

price charged for the like commodity to buyers in the domestic market, shall be considered not to involve a subsidy on export within the meaning of paragraph 1 of Article 26, if the organization determines that: (a) the system has also resulted, or is so designed as to result, in the sale of the commodity for export at a price higher than the comparable price charged for the like commodity to buyers in the domestic market; and (b) the system is so operated, or is designed so to operate, either because of the effective regulation of production otherwise, as not to stimulate exports unduly or otherwise seriously prejudice the interests of other Members. *The Havana Charter supra* note 67.

⁷² Chapter VI: Inter-Governmental Commodity Agreements. Section A – Introductory Considerations. Article 55. Difficulties Relating to Primary Commodities. *The Havana Charter supra* note 67.

⁷³ See The Havana Charter Art. 57.

⁷⁴ See The Havana Charter Art. 61 2(b).

at increasing consumption of agricultural products.⁷⁵ Chapter VI of the Havana Charter created a separate system for agricultural subsidies that was not incorporated by the *GATT 1947*. If it had been incorporated, distortions in the regulation of agricultural products would have tended to be even higher.

Art. 26 of the Charter limited export subsidies only in the situation where the export price was lower than that for a comparable domestic product. However, regarding agriculture, if a Member could not comply with this provision, it had two options. The first was to follow the procedures outlined in Chapter VI. The second was to be exempted from the regulation of Art. 26, but in this case, it would have to comply with Art. 28, which established that agricultural subsidies could not be applied in a manner that gave a “more than equitable share” of the world trade in that commodity to the subsidizing Member.⁷⁶ If the Member chose the first option but the procedures outlined in Chapter VI failed, it still could resort to Art. 28.

In practical terms, the Charter had less stringent regulations for agricultural subsidies than the *GATT 1947*. The provisions of Chapter VI were a diplomatic attempt to resolve the matter without the possible limitation imposed by Art. 28 (the “more than an equitable share” clause). If neither the provisions of Chapter VI nor those of Art. 28 could resolve the problem, the ITO should have had to determine what would be considered an “equitable share” of the world trade in the commodity concerned.

The Charter established some parameters to guide this determination: a) what the commodity’s share of world trade was during a previous representative period; b) an account of whether the share of the world trade of the concerned subsidizing Member was insignificant and, consequently, would have minor impacts on third Members; c) a comparison between the

⁷⁵ See The Havana Charter Arts 58, 59 and 60.

⁷⁶ See The Havana Charter Art. 28.

external trade in the commodity and the economies of the subsidizing and the materially affected Member; d) the existence of subsidies; and also e) the desire of the subsidizing Member to reduce subsidies.⁷⁷ Some of these parameters, such as a determination of a representative period of time, were later incorporated into the TRSC.

The Havana Charter established some criteria to help the panelists to define what would be an “equitable share.” There were subjective factors, such as the desire of the subsidizing Member to limit its support measures. Probably, if the Charter had been implemented, such factors would have made the definition of an “equitable share” difficult, and consequently, challengeability would have been difficult as well. The *GATT 1947* did not implement the subjective provisions of Chapter VI that created a separate system of regulation for agriculture and did not limit subsidization and kept the “more than equitable share” concept for the challengeability of agricultural subsidies. Because of these reasons, the regulation of agricultural subsidies in the *GATT 1947* was clearer and less subjective and distorted than it was in the Charter.

John Jackson stated that the modifications of the *GATT 1947* as a result of the ITO’s failure might be the reason that the *GATT 1947* was “overly rigid in many respects.”⁷⁸ Professor Jackson is suggesting that *GATT 1947* provisions had to have a flexible interpretation because they were “confining and restricting” in the sense that they were supposed to be a contract and not a whole system of regulation.

We can also conclude from his words and from the analysis above that the *GATT 1947* had more stringent provisions in some aspects of regulation than did the Havana Charter. Therefore, in terms of the challengeability of agricultural subsidies, the fact that the *GATT 1947*

⁷⁷ *Ibid* Art. 28:4 (a), (b), (c), (d) and (e).

⁷⁸ Jackson, *Law of GATT supra* note 68 at 49.

was created to be a contract and not an institution was not prejudicial in the sense that *GATT 1947* had more stringent provisions than did the Charter to avoid agricultural subsidization.

The *GATT 1947* cases not only helped to define the boundaries of some concepts, such as “more than an equitable share,” but they also developed a rationale against agricultural subsidization and, for this reason, made challengeability possible, as is going to be demonstrated in the two cases verified below.

I.2.2.1.1 The *France - Wheat Exports* Case and the Concept of “More than an Equitable Share of the World Export Trade”

The “equitable share” concept was analyzed in *France – Assistance to Exports of Wheat and Wheat Flour [France – Wheat Exports]*.⁷⁹ This case was emblematic, because it was evidence that agricultural subsidies could be challenged under the *GATT 1947* and that general terms such as “equitable share” were not an obstacle for any determination of the illegality of agricultural subsidization. In a report issued on November 21, 1958, the Panel for Conciliation examined a complaint made by the Government of Australia, who claimed that agricultural subsidies were being granted by the French government on exports of wheat and wheat flour and were inconsistent with the provisions of *GATT 1947* Article XIV:3. Australia alleged that the French exports had displaced Australian trade in these products, particularly in the markets of Ceylon, Indonesia and Malaya, and had impaired benefits accrued to Australia under the *GATT 1947*.

The panel examined the following legal issues: a) whether the French price equalization program for wheat and flour amounted to the granting of subsidies on exports of those products; b) whether France had gotten “more than an equitable share of the world trade” for these

⁷⁹ *France – Wheat Exports supra* note 64.

products, which would go against the provision of *GATT 1947* Article XVI; and c) to what extent the French equalization program had impaired the benefits accruing directly or indirectly to the Government of Australia under the *GATT 1947* through displacement.

The Panel for Conciliation found that the French agency *Office National Interprofessionnel des Cereales* [ONIC] controlled production, collection, storage and domestic sale of cereals, including wheat and wheat flour. ONIC also guaranteed prices to exporters that were lower than world prices, covering the difference. The consequence was that the prices charged for French exports of wheat flour had fallen, which was confirmed by the import unit values recorded in Ceylon, Malaya and Indonesia.

In 1954, France's share in world trade started to steadily rise and, despite a crop failure in 1956, France's exports of wheat accounted for 9 to 10% of world exports.⁸⁰ France responded that the country's status as an exporter of wheat and wheat flour had been recognized by the International Wheat Agreement [IWA], under which export quotas had been awarded to the country. France also claimed that its share in the world exports of wheat and wheat flour among the five major exporting countries (United States, Canada, Argentina, Australia and France) was significantly less if compared with the other big producers.

The panel made a consistent analysis of France's export quantity levels over the years and found that exports of wheat and wheat flour began to rise in 1954, substantially exceeding the quantities exported in any year since 1934. The panel found that this increase, in absolute quantities of wheat and wheat flour exported by France, meant an increase in France's share of world trade exports. It also approached the issue of whether this increase in France's share of world exports could be attributed to the French equalization programs. The panel concluded that the values of French exports of wheat and wheat flour were lower than those quoted by other

⁸⁰ *Ibid* at 3.

exports either in FOB or CIF⁸¹ values. It also found that the price of exports for wheat flour had considerably increased in the years prior to the panel's forming, even though the flour was exported from France at a cheaper rate than wheat. Meanwhile, exports of flour from Australia, Canada and the United States exceeded the export price of wheat in France by 30 to 50 percent.⁸² On the basis of this evidence "... the Panel concluded that the operation of the French system did in fact result in the grant of subsidies on the export of wheat and wheat flour within the terms of paragraph 3 of Article XVI."⁸³

The panel then analyzed whether the French equalization programs resulted in France's obtaining "more than an equitable share of the world export trade" in the wheat and wheat flour international market. The conclusion was that, even with no statistical definition of an "equitable share" in world exports, the French equalization subsidy programs contributed "to a large extent" to the increase in France's exports of wheat and of wheat flour. For this reason, the panel concluded that "the French share of world export trade, particularly in wheat flour, [was] more than equitable."⁸⁴

It is relevant to note that the first *GATT 1947* Article XVI case concerning agricultural subsidies clearly stated that one country's exports were getting "more than an equitable share of the world export trade." First, the Panel noted that there was not a crystal clear definition in Article XVI of what was an "equitable" share of world trade. However, it recalled that, at both

⁸¹ Incoterms are a universally recognized set of definitions of international trade terms, such as F.O.B and C.I.F. developed by the International Chamber of Commerce in Paris, France. F.O.B (*Free on Board*) is a term that designates the seller as responsible for the expenses generated with the delivery of goods on board the vessel at the named port of origin. The buyer is responsible for the main carriage/freight cargo insurance and other costs. CIF (*Cost, Insurance and Freight*) is a term that designates the seller as responsible for expenses for the cargo insurance and deliver of goods to the named port of destination. Buyer is responsible for the import customs clearance and other costs and risks. International Chamber of Commerce, *Incoterms: International Commercial Terms* (Paris: ICC, 2000).

⁸² *France – Wheat Exports supra* note 64 at 6, table II.

⁸³ *Ibid.* at 8 n. 33.

⁸⁴ *Ibid.* at 9.

Havana and the Review Section, when the provisions of this *GATT 1947* paragraph were discussed, it was agreed that the concept of an “equitable share” in world markets was meant to refer to a share in world export trade of a particular product and not to trade in that product in individual markets.

More importantly, the panel stated that it would have been understood in the review section that the *GATT 1947* contracting parties should not lose sight of the “desirability of facilitating the satisfaction of world requirements of the commodity concerned in the most effective and economic manner” and that due account should be taken of any “special factors affecting world trade in the products under reference with particular regard to the exporting country’s share of world trade in those products during a previous representative period.”⁸⁵

The panel interpreted agricultural subsidies on wheat and wheat flour in France as not having contributed to the world commercialization of these products in an effective and economic manner. It is relevant to note that general principles and *GATT 1947* material rules of Art. XVI were sufficient to condemn illegal agricultural subsidization. These principles guided the panel’s decision to declare that the French subsidy programs on wheat and wheat flour violated *GATT 1947* Art. XVI. The panel’s decision was also in accordance with the interpretation of the *GATT 1947*, that agricultural trade should be the least disruptive possible.

The panel also addressed the question of whether, and to what extent, the French subsidy programs on the export of wheat and wheat flour had caused injury to Australia. It also analyzed whether such injury represented an impairment of benefits accruing to Australia under the *GATT 1947*. France alleged that other factors had influenced the world market in wheat. It stated that Australia’s claim was not well founded, because the country could not supply the Asian wheat flour market, due to two consecutive short crops.

⁸⁵ *Ibid.* at 8.

The panel reached the conclusion that, even though it was difficult to estimate the level of displacement, it was clear that French supplies had largely displaced Australian supplies in the three markets and, consequently, had caused injury to Australia. This *GATT* decision was clear and precise in determining that French agricultural subsidies had displaced Australian exports in Southeast Asia, according to the legitimate evidence⁸⁶ presented by Australia. It is relevant to note that, according to the panel, displacement⁸⁷ was not a requirement for the “more than an equitable share” concept, even though displacement could be proved as well.

Vague legal concepts such as “equitable share” were not an obstacle to challenge agricultural subsidies under the *GATT 1947*. Furthermore, this decision was precise in condemning agricultural subsidies if compared with several others challenging agricultural subsidies under the *AoA* and *SCM Agreement* after the creation of the WTO that will be further analyzed in the next chapters of this thesis..

The legal decision established by *France – Wheat Exports* was important in establishing the line of judgment for subsequent GATT cases that were not favorable to agricultural subsidization. The decision was made according to the concept of “equitable share” as a share in world export trade of a particular product and not trade in that product in individual markets. This rationale for condemnation was dominant in later disputes acting under *GATT 1947* Article

⁸⁶ It was relevant for this finding of the panel that the French total wheat flour exports rose from 13% in 1953-34 to 34% in 1957-58, while Australia’s exports to these markets fell substantially during the same period, and their share in Australia’s total exports of wheat flour declined from 64% in 1953-54 to 50% in 1957-58. The other significant change was the proportion of French supplies in the total imports of wheat consumed in the Southeast Asian markets. The French supplies peaked from 0.7% to 46% in the first half of 1958. On the other hand, the Australian supplies fell from 83% in 1954 to 37% in the first half of 1958. *France – Wheat Exports supra* note 57 at 5-6.

⁸⁷ Marc Benitah also states that displacement was not a requirement for the *more than an equitable share* concept: In the first stage, relating to the determination of the “equitable” or “inequitable” nature of France’s market, share, the Panel did not apply the “displacement in a specific market” criterion. Rather, having only found a correlation between a modification of world market shares and the French export subsidies system, the Panel thereby concluded that it was “reasonable” to deduce from this correlation that the French world market share at that time was “more than equitable.”

Marc Benitah *The Law of Subsidies under the GATT/WTO System*. (The Hague; Boston; Kluwer Law International, 2001) at 176 [Benitah, *Law of Subsidies*].

XVI, but the new Code on Subsidies brought about by the Tokyo Round linked the concept of “equitable share” to the market effect requirement of “displacement,” which raised the threshold for the challengeability of agricultural subsidies, as is going to be seen.

I.2.2.1.2 The *EC – Sugar Exports* Cases and the Link Between the Concept of “Equitable Share” and “Displacement” under the TRSC

Two parallel complaints, challenging EC subsidies for sugar, were filed almost at the same time by Australia and Brazil. In the *European Communities – Refunds on Exports of Sugar* [*EC – Sugar Exports*] cases,⁸⁸ the complainants challenged the legality of the EC sugar export subsidy programs. Both countries alleged that these programs gave to the EC more than an “equitable share of world export trade” in the sugar market, which was a violation of *GATT 1947* Article XVI:3. The legal claims of the cases challenged the main aspects of the EC Common Agriculture Policy.

In both cases, illegal agricultural subsidization of sugar was condemned, and the decisions held that European support programs for sugar had caused serious prejudice to the complainants. However, in both cases, the panels were not able to declare that these subsidies had given “more than an equitable share of the world trade” in sugar to the EC. The failure to make such determination was mainly due to the successful European allegation – influenced by the negotiations of the TRSC that would later be concluded – that displacement should be proved in specific markets for a condemnation of illegal subsidization under *GATT 1947* Art. XVI. When the case was decided, the TRSC was being implemented.⁸⁹ The EC also convinced the

⁸⁸ *EC – Sugar Exports (Australia)* *supra* note 54 and *EC – Sugar Exports (Brazil)* *supra* note 54. The interesting point was that two different panels were established, but identical Members were appointed to decide the cases. The Australian complaint was decided in October 1979, and the Brazilian complaint one year later.

⁸⁹ In 1979, the TRSC had been implemented by some countries. Therefore, the panel noted that the parties in the dispute had accepted the Code and mentioned Art. 10:2(a) and (b) of the TRSC, which established that “more than

panel of the existence of other complex market-effect factors, in addition to the EC sugar programs, that distorted the international sugar market.

In *France – Wheat Exports*, it was possible to prove that France had obtained “more than an equitable share” of the wheat flour market. At that time, displacement was not a requirement for challengeability under *GATT 1947* Art. XVI, which established that exports could not give “more than an equitable share of the world export trade” to the subsidizing Member. However, in the *EC – Sugar Exports* cases, the panels were influenced by the new provisions of the TRSC, which established that displacement was a requirement for challengeability under *GATT 1947* Art. XVI, and therefore, they declined to rule on this specific matter because of the complexity of the economic analysis to prove displacement. In order to prove displacement, econometric calculations are necessary.

It is important to note, however, that the panels’ declining to rule on the “equitable share” clause did not hinder the panelists from condemning European subsidies of sugar and declaring that they had caused adverse effects to the complainants. The panels found evidence that European agricultural subsidies had given more than an “equitable share of world export trade” to the EC. The EC did not deny its high level of agricultural subsidization. Following the legal rationale in *France – Wheat Exports*, the panels’ decision held that European subsidies had depressed world sugar prices and had caused economic injury to the complainants.

Australia and Brazil claimed that the EC’s system of sugar-export subsidies had given “more than an equitable share of the world export trade” in sugar to the European Community.

an equitable share” of world export trade should include displacement of the exports of another signatory. This was the first occasion that the concept of displacement was included as a requirement for challengeability in *GATT 1947* Art. XVI because of the new provisions of the TRSC. The result was that, even though the panel found that there was a change in the relative positions of Brazil and EC in the sugar market, its systematic analysis could not provide clear and general evidence that Brazilian supplies had been directly displaced by subsidized exports of Community’s Sugar in specific markets. *EC – Sugar Exports (Brazil) supra* note 54 at para. 4.15.

For this reason, the subsidies had caused or threatened serious prejudice to Australian and Brazilian commercial interests and had nullified or impaired benefits accruing either directly or indirectly to Australia and Brazil under the *GATT 1947*.⁹⁰ There was evidence that the EC's price support had driven sugar prices far below world market prices. The EC subsidies had artificially stimulated production above ordinary levels of national consumption. For this reason, surpluses had to be exported, which created unfair competition. The legal argument of Australia and Brazil was that the EC's share of the world market had increased from 8.3% before 1976 to 14.4%, in 1978, and such impressive growth had been achieved because of EC export subsidy programs.⁹¹

High European costs of production meant that substantial export subsidies were needed in order to compete in the world market; otherwise, the EC would not be able to export its sugar. Brazil and Australia were trying to prove that the EC had "more than an equitable share" of the international sugar market, since the increase in its primary exports was artificial. Even though it is difficult to define what "equitable" meant, the *France –Wheat Exports* case had already proven that this concept can be determined. Besides, it could be stated that "equitable" means something close to the normal market share that a country would have without the use of subsidies.⁹²

The problem was that the panel used as reference the TRSC concept of "equitable share," which had already established displacement as a requirement for the challengeability of agricultural subsidies. Therefore, econometric calculations had to be done in order to determine

⁹⁰ It is interesting to note that even cases of *GATT 1947* Art. XVI were also brought under Art. XXIII because subsidies normally nullified or impaired benefits and it is going to be verified that the threshold of challengeability of agricultural subsidies of *GATT 1947* Art. XVI is higher than Art. XXIII. See *EC – Sugar Exports (Australia)* *supra* note 54 and *EC – Sugar Exports (Brazil)* *supra* note 54.

⁹¹ *Ibid.* at 19.

⁹² See Hudec, *Enforcing Trade Law* *supra* note 17.

how external factors contributed to the displacement, and it became difficult to determine what would be a normal market without subsidies.⁹³

When the panel had to deal with the concept of “displacement” in specific markets to define the concept of “more than an equitable share” concept, it found a problem that could not be solved, as Professor Benitah explained⁹⁴, because the panel did not have the tools to investigate causality in each affected market.

There were several market-distorting practices that interfered with the prices adopted by most participants in the sugar market. Despite various national and international distortion factors in this market, the main producers had signed the International Sugar Agreement [ISA]⁹⁵ which set limitations on supplying sugar and which had raised sugar prices. The market was also influenced by other side agreements⁹⁶ that had been negotiated for large quantities of sugar and other long-term supply arrangements that could interfere with the prices. Because these side agreements entered into effect outside *GATT 1947* obligations, it was more difficult to delineate on what level subsidies from one specific country could interfere with world market prices.

The EC argued that complainants had not succeeded in demonstrating the cause-and-effect linkage between EC exports and their market losses, even though this linkage was not a requirement for challengeability during the GATT years. The EC’s approach was not to deny its high level of agricultural subsidization, but rather to assert that it was substantially difficult to

⁹³ “In Sum, once the Panel adopted the ‘displacement in specific markets’ criterion in the very definition of the ‘more than an equitable share’ concept, it was condemned to quasi-insoluble causality problems due to the interplay of various factors and to the fact that these markets may have changed significantly in size and nature”. Benitah, *Law of Subsidies supra* note 87 at 178.

⁹⁴ *Ibid.*

⁹⁵ The 1977 International Sugar Agreement is one of several contemporary agreements designed to regulate the international market in specific commodities. A commodity agreement, at the same time, serves as an instrument through which nations’ international policies are carried out and defines the rights and duties characterizing the relations between importing and exporting countries. Khan, K. “The International Sugar Agreement 1977 – Market and Instrument of International Policy” (1978) 3 Food Policy 104.

⁹⁶ International Sugar Organization, “Sugar Yearbook 1977”, No. 31 (1978), online: International Sugar Organization <<http://www.isosugar.org/SYB.htm>>

clearly define the market share of any GATT contracting party. They alleged that almost every player in the world sugar market had some kind of distortive financial aid. The EC could not prove that its subsidies were not distorting the international sugar market. Therefore, their strategy was to make the legal analysis of the panel difficult through the allegation that not only European subsidies but also other exogenous market-effect factors had contributed to the distortions in the international sugar market.

The EC representative argued that there was no clear relationship between an increasing amount of subsidies and the expansion of exports. According to his reasoning, the amount of subsidies could not constitute a useful element of interpreting Article XVI:3.⁹⁷ Furthermore, the representative stated that it could not be proven that the price of the product exported by the EC had been brought to a level below that of the world price as a result of the EC's subsidies.⁹⁸

Brazil and Australia used the ISA of 1977, which was not signed by the EC and under which Member countries voluntarily restrained exports to raise prices, as the basis for the argument that the EC was obstructing efforts to stabilize the world market. As a response to this line of argumentation, the EC's representative only stated that "...with regard to Community participation in the International Sugar Agreements, there was no use in recalling the reasons for the present state of affairs."⁹⁹ The representative questioned the concept of "equitable share" and gave the example of *France – Wheat Exports*, recalling that "... at both Havana and the ninth section when the provisions of paragraph 3 of Article XVI were discussed, it was implicitly

⁹⁷ *EC – Sugar Exports (Brazil) supra* note 54 at 3.

⁹⁸ *Ibid.* at 4.

⁹⁹ *Ibid.* at 9.

agreed that the concept of 'equitable share' was meant to refer to share in 'world' export trade of a particular product and not to trade in that product in individual markets."¹⁰⁰

The panel held that its examination should not be based on the concept of the "free market" introduced by Australia in paragraph 2.20,¹⁰¹ but on the concept of the "world export trade" mentioned in *GATT 1947* Article XVI:3, according to previous contracting parties' discussions.¹⁰² The result was that the panel decided to verify the "equitable share provision" through an analysis of displacement based on specific markets and not on the "whole export trade market" in a particular product. Therefore, because methodological difficulties would make any comparison difficult, meaning that the panel at the time was not able to analyze the complex market-effect factors that might or might not have influenced the sugar world market, the panel declined to decide whether a market share was a "more than equitable share of world export trade."

As has been seen, the concept in *France – Wheat Exports* was meant to refer to a share in "world" export trade in a particular product and not to trade in that product in individual markets. But in *EC – Sugar Exports*, the panel approached the concept of "equitable share" through an analysis of displacement based on specific markets and not on the "whole export trade market." The interpretation that the panel used was difficult to be proved because an individual analysis of displacement in each affected market was necessary. Conversely, if the interpretation used in

¹⁰⁰ In this particular issue, it is relevant to stress that in *France –Wheat Exports* the panel constructed its legal analysis taking into account that the Asian market was the main market for displaced exports of the complainants. *France – Wheat Exports* note 64 at 9.

¹⁰¹ "The Australian representative argued that when looking at EC sugar export practices, Australia and other contracting parties should be concerned with the "world free market". This was the only export market accessible to both Australia and the European Communities and the only market accessible to all exporters on the basis of open competition and where, in consequence, the price effects of such competition occurred. In his view, that was the GATT sense of "world export trade"". *EC – Sugar Exports (Australia) supra* note 54 at 5-6 para. 2.20.

¹⁰² GATT, *Discussions at the ninth section of the Contracting Parties*, GATT SR. 9/41 of 15 March 1955 at 6, online: WTO http://www.wto.org/gatt_docs/English/SULPDF/90270355.pdf and *France - Wheat Exports supra* note 57.

France – Wheat Exports had been used, only the exports of a particular product had to be examined. In this way, perhaps, the concept of “more than an equitable share” could have been proved in this case. The point is that, when displacement was not at stake, the “equitable share” of a product exported by a Member could be verified through an analysis of variation of market shares in world export trade.

However, such analysis was not sufficient to prove displacement. Under the interpretation of this panel, individual markets had to be analyzed in order to examine whether exports of a product were displaced by exports of the like product by another Member. The establishment by the TRSC of “displacement” was a requirement to prove that a country had obtained more than an “equitable share” of the world export trade in a product, higher than the threshold of challengeability of agricultural subsidies. Therefore, this was the predominant reason that the panel in this case did not declare that EC subsidies had given to them more than an equitable share of the world export trade in sugar.

The panel reasoned that no definition of “equitable share” had been provided and that, in the past, a precise definition of the concept had not been considered absolutely necessary. Therefore, the panel stated that in this case it would be sufficient to try to analyze the “main reasons for developments in individual market shares, and to examine market and price developments, and then draw a conclusion on that basis.”¹⁰³ This was relevant, because the panel was stating that, if there was serious evidence or proof of illegal subsidization, there was no need for exact and precise terms for successful challengeability. The principles and the substantive rule established under *GATT 1947* Art. XVI was enough.¹⁰⁴

¹⁰³ *EC – Sugar Exports (Brazil)* *supra* note 54 at para. 4.11.

¹⁰⁴ Later the *US – Upland Cotton* *supra* note 14 reached a similar conclusion condemning American subsidies on cotton but without ruling whether they had given to the US more than an equitable share of the world export trade on cotton.

It seems that the panel was contradicting itself. At the same time that it could not decide whether a market share was a “more than equitable share of world export” trade because of methodological difficulties; it stated that a precise definition of “equitable share” was not decisive for the decision at hand. Actually, it was not a contradiction, because the panelists held that a clear definition of “equitable share” was not needed to condemn illegal subsidization. However, in this specific case – because the panel was not able to analyze complex market-effects that might have interfered in the international sugar market in specific markets as required by the concept of displacement – it was not possible to determine if the EC had gotten “more than an equitable share of the world export trade.” In opposition, when this concept was not linked with the concept of displacement, which allowed the verification of the “whole export market” in a specific product, this verification was possible. Therefore, we can imply that the problem was not the inaccuracy of the term in *GATT 1947* Art. XVI, but the institution of “displacement” to prove “equitable share” brought in by the TRSC.

However, the European strategy of making the legal analysis of the panelists difficult by including as many economic variables as possible as factors that had distorted the market did not completely succeed. Even though the panel was not able to declare that European subsidies had given to the EC more than an equitable share of the world export trade in sugar, the panel held that European subsidies, in this case, had contributed to depressing world sugar prices and had caused serious prejudice to the interests of Australia and Brazil.

“... the Panel found that it was not in a position to reach a definite conclusion that the increased share had resulted in the European Communities "having more than an equitable share of world export trade in that product,¹⁰⁵" in terms of Article XVI:3. ...The

¹⁰⁵ Although the cases were not brought under the new Subsidies Code, it seems that the panels were applying the Code’s new displacement test. Actually, some words in the panel reports were very similar to words used in the Code’s Article 10:2(a), such as the new “displacement” and “equitable share.” The same happened in the Brazilian

Panel noted however that the Community system for granting refunds on sugar exports and its application had contributed to depress world sugar prices in recent years and that thereby serious prejudice had been caused indirectly to Australia, although it was not feasible to quantify the prejudice in exact terms.”¹⁰⁶

This case proves that displacement was not a requirement to prove serious prejudice under the *GATT 1947*, and the link established by the TRSC between “displacement” and the concept of “more than an equitable share of the world export trade” made challengeability of agricultural subsidies more difficult. This conclusion is reached because the panel declared that EC subsidies were causing serious prejudice to other exporters of sugar.

At that time, however, the only consequence of a “serious prejudice” ruling was an obligation to consult on how the subsidy might be limited, with no further obligation.¹⁰⁷ Even so, the panel did hold that European subsidies had depressed world sugar prices and had caused economic injury to the complainants. The legal analysis of the panel was consistent and sufficient to condemn European subsidies and make retaliation from the complainants possible. If compensation or retaliation did not occur, it was not for legal reasons.¹⁰⁸

As has been seen in this case, the TRSC negotiated in the Tokyo Round and implemented by some signatories influenced challengeability of agricultural subsidies in a negative way. The reason was that little was done in terms of agricultural liberalization or innovation on substantive

complaint quoting Subsidies Code Article 10.2(a). *EC – Sugar Exports (Brazil)* supra note 54 at para. 4.71 and *EC – Sugar Exports (Australia)* supra note 54 at para. 4.13.

¹⁰⁶ *EC – Sugar Exports (Brazil)* supra note 54 at 25.

¹⁰⁷ GATT, *Minutes of Meeting, held in the Centre William Rappard*, C/M.156 (31 March 1982) online: WTO http://www.wto.org/gatt_docs/English/SULPDF/90440041.pdf.

¹⁰⁸ Some scholars asserted that panel was also looking for a way to avoid a ruling that would very likely have triggered an explosive confrontation between GATT and the European Community. Such confrontation at that time could damage the GATT structure. Some of them say that the EC would never accept a ruling invalidating one of the most important policy instruments of its Common Agricultural Policy. Hudec, *Enforcing Trade Law* supra note 17 at 133

rules, and challengeability became more difficult because of the market-effect requirements that the Code implemented to challenge agricultural subsidies.¹⁰⁹

I.3 The Tokyo Round

The Tokyo Round¹¹⁰ officially started in the fall of 1973 at a meeting of GATT ministers in Tokyo. The negotiations were difficult because of a fierce divergence of interests on agricultural policies between the two major forces in the GATT years: the US and the EC. Agriculture was considered one of the failures of the Round.¹¹¹ This was one of the reasons for the timid advance regarding substantive regulation of agricultural subsidies in the Tokyo Round Subsidies Code.

The Tokyo Round was different from the previous GATT rounds because it emphasized the negotiation of non-trade barriers,¹¹² perhaps because the preceding rounds had succeeded in

¹⁰⁹ On the Note of the Secretariat of the Draft Report of the Committee on Trade in Agriculture from 13 February 1984 it was observed that “the Subsidies Code had been negative as far as improving the disciplines of Article XVI and making its interpretation more precise.” *GATT CTA Report supra* note 51 at para. 39.

¹¹⁰ The negotiations were called “Tokyo Round” because the ministerial Meeting that decided on the Round was held in Tokyo although the negotiation took place in Geneva. It lasted from 1973 to 1979.

¹¹¹ Robert Hudec explains the results of the Round in his opinion:

There were several important defeats [in the Tokyo Round]. Perhaps the most important was agriculture, which had become an increasingly important issue as the Tokyo Round wore on... [a]part from certain bilateral concessions on particular products, the only results of these long and bitter negotiations were the Dairy and Bovine Meat Agreements, both of which were designed to accomplish price maintenance than trade liberalization. The next most important failure, also related to agriculture, was the failure of the United States’ effort to establish stronger discipline over domestic and export subsidies.

Hudec, *Enforcing Trade Law supra* note 17 at 133 at 27.

¹¹² The term non-tariff barriers was not defined in any GATT’s document. Hillman define the term as:

[A]ny governmental device or practice, other than a tariff which directly impeded the entry of imports into a country and which discriminates against imports ... non-tariff measures include several types of policies or practices which interfere with or distort trade: (1) measures which restrict imports; (2) measures which provide assistance to domestic production in order to substitute for imports, and which, in effect, promote exports; and (3) measures which provide direct assistance to exporters.

Jimmye S. Hillman, *Non-tariff Agricultural Trade Barriers* (Lincoln:Univerisity of Nebraska Press, 1978) at14. They can be quotas, tariff rate quotas, subsidies and other market distorting practices.

reducing tariffs. Subsidies disciplines, which are one of the most important non-tariff measures, benefited from this shift in the negotiations.

During the Round, there was a perception that government involvement was growing in the area of international trade. For this reason, there was consensus that agreements should be reached, in order to avoid conflicts in the future.¹¹³ From the beginning of the Round, subsidies were at the centre of the negotiations, marked by conflicts of interest between the US and the EC. The former kept an offensive position on the reform of agriculture, because it was concerned with the severe tariff and non-tariff restrictions of the EC.

During the Round, there were difficulties in the agricultural negotiations, mostly because of the Common Agricultural Policy [CAP] of the EC, which allowed high levels of subsidization for European farmers and widely restricted primary imports to Europe. However, even with the problems in the agricultural negotiations, the Agreement¹¹⁴ which regulated subsidies was finalized: the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the *General Agreement on Tariffs and Trade*, the so called Tokyo Round Subsidies Code..¹¹⁵

I.3.1 The Tokyo Round Subsidies Code and the Market-Effect Requirements

The battle between major forces described above had a negative impact on the TRSC.¹¹⁶ The EC succeeded in its goal to make the challengeability of agricultural subsidies more

¹¹³ R.R. Rivers & J.D. Greenwald. "The Negotiation of a Code on Subsidies and Countervailing Measures: Bridging Fundamental Policy Differences" (1979) 11 *Law and Policy in International Business* 1447 at 1452 [Rivers, "Code on Subsidies"].

¹¹⁴ Other agreements were also negotiated during the Tokyo Round. These agreements covered quite a large series of different subjects: there was a new improved Anti-dumping Code, Custom valuation, Import Licenses, Technical Barriers to Trade and a Code on Government Procurement.

¹¹⁵ GATT, *Agreement on Interpretation and Application of Articles VI, XVI, and XXIII of the General Agreement on Tariffs and Trade* 26th Supp. B.I.S.D. (1980) 56-83 [TRSC].

¹¹⁶ See *supra* note 19.

difficult,. Even though there were some advances in some procedural rules – especially for countervailing duties and dispute settlement – the code represented a step backwards in terms of possible challengeability for agricultural subsidies. The problem was that the code imposed higher and more complex thresholds for challengeability of agricultural subsidies.

This section will describe the new proposed rules in the TRSC and compare it with the *GATT 1947*'s and the WTO's regulations for agricultural subsidies. The goal is to make a comparative legislative analysis to study what exactly changed in the TRSC from the *GATT 1947* legislation (especially Art. XVI) and what the influence of the code was on further WTO legislation (especially the *SCM Agreement* and the *AoA*) in terms of challengeability for agricultural subsidies.

The TRSC drafted during 1975–1979 soon incorporated the basic structure of the *GATT 1947* (Articles XVI:3 and XVI:4) for subsidies, with some modifications and clarifications. The modifications on subsidies' discipline were placed alongside the new rules governing countervailing duties. The code contained a large number of provisions¹¹⁷ on procedural rules on subsidies but few substantive innovations compared with the *GATT* disciplines.¹¹⁸ For example, the TRSC did not regulate or define the concept of “subsidy” itself, which was done later under the *SCM Agreement*.

Part I of the TRSC regulated the application of Article VI of the *GATT 1947*,¹¹⁹ and Part II established rules on subsidies in general. Part I covered countervailing duties, regulating how national governments should apply countervailing duty rules and in which cases they should refrain from using the procedures for those countervailing duty cases. It clearly established that an investigation should only be initiated upon a written request, under the evidence of a) subsidy,

¹¹⁷ The TRSC has 19 articles divided in seven parts and also has an illustrative list of export subsidies.

¹¹⁸ The dispute settlement procedure was the most significant legislative innovation brought by the TRSC.

¹¹⁹ See *GATT 1947* provision on Anti-Dumping and Countervailing Duties.

b) injury according the meaning of *GATT 1947* Art. VI and c) a causal link between the subsidy and the alleged injury.¹²⁰ *GATT 1947* Art. VI 6 (a) had established that countervailing duties should only be applied when there was material injury. The TRSC kept this provision, adding the need to prove a causal link between the subsidy and the injury, which raised the threshold to countervail subsidies.

The TRSC developed a more elaborated and complex concept of injury,¹²¹ later applied in the *SCM Agreement*. It linked the concept of injury to the volume of subsidized imports and to the consequent impact of these imports on domestic producers.¹²² It determined that an examination of the impact on domestic industry should include an evaluation of several market-effect factors, such as potential decline in sales, market share, profits, productivity, return on investments and other factors.¹²³ This TRSC was the basis for subsidies' challengeability through countervailing duties that was later applied in the *SCM Agreement*.

TRSC Part II, Art. 7, paragraph 1 established that any signatory "may make a written request" for information on the nature and extent of any subsidy granted or maintained by another signatory that directly or indirectly increased exports of any product from or reduced imports of any product to its territory.¹²⁴ In this case, the language of *GATT 1947* Article XVI was more stringent, because Art. XVI established that any contracting party *shall* (not "may," as was stated in the TRSC) notify in writing the extent and nature of the subsidization.

TRSC Part II, Art. 7, paragraph 2 added some elements on timing and *modus operandi* to the *GATT 1947* regulation. For example, it added that the information provided on subsidies

¹²⁰ See TRSC Art. 2.1.

¹²¹ *GATT 1947* Art. VI 6(a) establishes that "no contracting party shall levy any anti-dumping or countervailing duty on the importation of any product of the territory of another contracting party unless it determines that the effect of the dumping or subsidization, as the case may be, is such as to cause or threaten material injury to an established domestic industry, or is such as to retard materially the establishment of a domestic industry."

¹²² See TRSC Art. 6.1.

¹²³ See TRSC Art. 6.3.

¹²⁴ See TRSC Art. 7, Paragraph 1.

specified in *GATT 1947* Art. XVI should be given “as quickly as possible,”¹²⁵ and if such information was not promptly delivered, the signatory could bring the subsidy practice “to the notice of the Committee.”¹²⁶ The goal was to explain and give more accuracy to some *GATT 1947* terms on subsidy regulation, which did not occur because a term such as “as quickly as possible” was not precise, either.

Art. 8 established that the use of subsidies could cause adverse impacts to signatories through injury, nullification or impairment of any benefit or serious prejudice to the interests of any other signatory.¹²⁷ Later, the *SCM Agreement* Art. 5 defined adverse effects in almost identical words. The difference was that the *SCM Agreement* clearly stipulated that Art. 5 did not apply to agricultural products according to *AoA* Art. 13, because of the shield of the Peace Clause.

Paragraph 4 of TRSC Art. 8 declared that the adverse effects required to demonstrate nullification or impairment or serious prejudice could arise a) through the effects of the subsidized imports on the domestic market of the importing country, b) through the effects of the subsidies in displacing or impeding the imports of a like product into the market of the subsidizing country, and c) through the effects of the subsidized exports in displacing the exports of like products of another signatory from a third country market.¹²⁸ This was the first time that the concept of displacement was included as a requirement to prove serious prejudice in the sense of *GATT 1947* Art. XVI. It raised the threshold for challengeability, as was demonstrated in by the *EC –Sugar Exports* cases and is going to be demonstrated in the analysis of the cases

¹²⁵ See TRSC Art. 7, Paragraph 2.

¹²⁶ See TRSC Art. 7, Paragraph 3.

¹²⁷ See TRSC Art. 8.3 (a), (b) and (c).

¹²⁸ See TRSC Art. 8.4 (a), (b) and (c).

below. Later, the *SCM Agreement* would raise the standards again, adding some other market-effect requirements to prove serious prejudice.

Regarding agricultural subsidies, TRSC Art. 9 established that signatories should not grant export subsidies on products other than *certain* primary products,¹²⁹ thereby allowing export subsidies for certain agricultural products listed in an illustrative annex of the Agreement.

Part II of the TRSC also reinforced a signatory's legal obligation to avoid the use of agricultural¹³⁰ export subsidies. Art. 10 established that, should a signatory grant any form of export subsidy that increased the export of a primary product, such subsidy should not be applied in a manner that resulted in the contracting party's having "more than an equitable share of world export trade in that product."¹³¹

In practical terms, the TRSC kept a regime similar to that of the *GATT 1947* for agricultural subsidies' regulation. The main difference was in TRSC Art. 10.2, (a), (b) and (c), which tried to define in detail the meaning of the term "more than an equitable share." The term was exhaustively debated, but no conclusion on the exact meaning was reached. The EC did not accept any broader concept of the expression. However, Tokyo Round negotiators from other countries did succeed in adding three paragraphs to Art. 10:2 that tried to help to define the term "more than an equitable share."¹³²

¹²⁹ TRSC Art.9.1 established that:

In accordance with the provisions of Article XVI:3 of the General Agreement, signatories agree not to grant directly or indirectly any export subsidy on certain primary products in a manner which results in the signatory granting such subsidy having more than an equitable share of world export trade in such product, account being taken of the shares of the signatories in trade in the product concerned during a previous representative period, and any special factors which may have affected or may be affecting trade in such product.

¹³⁰ Export subsidies on certain primary products according to the TRSC. See *supra* note 64.

¹³¹ See *GATT 1947* Art. XVI B 3.

¹³² See TRSC Art. 10:2(a)

The first paragraph¹³³ established that “more than an equitable share of world export trade” should include any situation where the effect of an export subsidy granted by a given signatory resulted in the displacement of another signatory’s exports. The TRSC established that displacement was a formal requirement for challengeability under the “equitable share” reasoning, which made challengeability more difficult because of the econometric evidence involved. Later, in 1995, the *SCM Agreement* established that serious prejudice would be attributed to any case of import displacement by a subsidizing Member¹³⁴ as well as in cases of export displacement in a third Member.¹³⁵

The second paragraph established that traditional patterns of the region and country in which the new market was situated should be taken into account in determining “equitable share of world export trade.” Although, it is difficult to precisely determine the intention of the signatories in this paragraph, it seems that “new market” encompassed a new area reached by the exports of the subsidizing signatory. If so, it would seem that the inclusion of this paragraph was intended to establish that the concept of equitable share was dependent upon the region of the country that was subject to harm by the subsidized imports.

Lastly, the third paragraph defined “a previous representative period”¹³⁶ used for analysis of whether a signatory had been harmed by subsidized primary exports as the “three most recent calendar years.” The same period of time was later included in the *AoA*.¹³⁷

Another limitation for export subsidization of agricultural subsidies contained in TRSC Art. 10 was established in paragraph 3, which stated that signatories agreed not to give subsidies

¹³³ *Ibid.*

¹³⁴ See *SCM Agreement* A 6.3. (a).

¹³⁵ See *SCM Agreement* A 6.3 (b).

¹³⁶ See *GATT 1947* Art. XVI B 2.

¹³⁷ “[T]he effect of the subsidy is an increase in the world market share of the subsidizing Member in a particular subsidized primary product or commodity as compared to the average share it had during the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted”. See *AoA* 6.3 (d).

on export of certain primary products in a manner that would result in prices materially below those of other suppliers to the same market. This limitation was based on *GATT 1947* Art. XVI, paragraph 4, which stated that, from January 1, 1958, contracting parties should cease to subsidize any product other than a primary product whose export would result in the sale of such product at a price lower than the comparable price charged for the like product to buyers in the domestic market.¹³⁸

The Report of the Committee on Trade and Agriculture stated in 1983 that TRSC Art. 10:3 “had not grappled satisfactorily with the price impact of export subsidies.” The problem was that the provision prohibited export subsidization for agricultural products in a manner that resulted in prices materially below those of other suppliers in the market but did not take into account distorted markets that could already have had prices below the market price. For this reason, the report stated that TRSC “Art. 10 had fallen short of the clear guidance as regards Article XVI that its drafters had hoped they would achieve.”¹³⁹

The provisions on export subsidies in both Agreements were similar. Neither the *GATT 1947* nor the TRSC prohibited export subsidies for agricultural products, but these subsidies could not give “more than an equitable share of the world trade” in the subsidized product to the subsidizing country¹⁴⁰ and could not result in sales with prices materially below those of the same product in the domestic market. Therefore, in terms of the challengeability of agricultural subsidies, the TRSC’s substantive provisions did not evolve much from the *GATT 1947*’s.

¹³⁸ See *GATT 1947* Art. XVI B 4.

¹³⁹ *GATT CTA Report supra* note 51 at 63.

¹⁴⁰ See *GATT 1947* Art. XVI 4. “... contracting parties shall cease to grant either directly or indirectly any form of subsidy on the export of any product other than a primary product which subsidies results in the sale of such product for export at a price lower than the comparable price charged for the like product to buyers in the domestic market....”

Art. 11 of the TRSC, dubbed “Subsidies Other Than Export Subsidies,” was the first provision to regulate the general discipline of governmental use of domestic subsidies in the legal framework of international trading. Art. 11 stated that domestic subsidies “are widely used for the promotion of social and economic policy objectives,” which partially justified the use of domestic subsidies. The TRSC set forth a *numerus clausus*¹⁴¹ list of circumstances under which subsidies could be used for social, economic and development purposes. This list helped to form the definition of non-actionable subsidies in *SCM Agreement* Art. 8,¹⁴² which expired at the end of 1999 and had similarities with the *AoA Annex II*,¹⁴³ which exempted agricultural domestic support from reduction commitments (green-box subsidies).

The TRSC 11:2 recognized that domestic subsidies, even though they were important instruments for social and economic development, “may cause or threaten to cause injury” to the domestic industry of other signatories, cause “serious prejudice to the interests” of other

¹⁴¹ The subsidies list described in the TRSC:

Art. 11:1. Signatories recognize that subsidies other than export subsidies are widely used as important instruments for the promotion of social and economic policy objectives and do not intend to restrict the right of signatories to use such subsidies to achieve these and other important policy objectives which they consider desirable. Signatories note that among such objectives are: Subsidies other than Export Subsidies: (a) the elimination of industrial, economic and social disadvantages of specific regions; (b) to facilitate the restructuring, under socially acceptable conditions, of certain sectors, especially where this has become necessary by reason of changes in trade and economic policies, including international Agreements resulting in lower barriers to trade; (c) generally to sustain employment and to encourage re-training and change in employment; (d) to encourage research and development programmes, especially in the field of high-technology industries; (e) the implementation of economic programmes and policies to promote the economic and social development of developing countries; (f) redeployment of industry in order to avoid congestion and environmental problems.

¹⁴² *SCM Agreement* Art. 8.2:

Notwithstanding the provisions of Parts III and V, the following subsidies shall be non-actionable: (a) assistance for research activities conducted by firms or by higher education or research establishments on a contract basis with firms if ... (b) assistance to disadvantaged regions within the territory of a Member given pursuant to a general framework of regional development and non-specific (within the meaning of Article 2) within eligible regions provided that ... (c) assistance to promote adaptation of existing facilities to new environmental requirements imposed by law and/or regulations which result in greater constraints and financial burden of firms, provided that the assistance ...”

¹⁴³ *AoA Annex 2.2*:

General services ... (a) research, including general research, research in connection with environmental programmes ... (b) pest and disease control ... (c) training services ... (d) extension and advisory services, including the provision of means to facilitate the transfer of information ... (e) inspection services, including general inspection services and the inspection of particular products for health, safety, grading ... (f) marketing and promotional services ... (g) infrastructural services ...”.

signatories or “may nullify or impair benefits” to the other signatories. Furthermore, there was the recommendation to “seek to avoid such effects through the use of subsidies.”

The TRSC systematized and divided into three types the harmful effects of subsidies. Injury was a concept based on *GATT 1947* Art. VI, serious prejudice was applied in the TRSC in the same sense it was used in *GATT 1947* Art. XVI:1 and nullification and impairment of any benefit accruing directly or indirectly to another signatory were taken from *GATT 1947* Art. XXIII 1(b). The impaired benefit included the benefits of tariff concessions, as TRSC footnote 24 stated. The TRSC systematized the harmful effects from subsidization but did not add any new concepts. All three types of effects mentioned in the TRSC were concepts conceived of by the *GATT 1947*.

The end of paragraph 2 stated that signatories, in order to avoid subsidies that caused adverse effects, had to take into account “the conditions of world trade, production (e.g., price, capacity utilization, etc.) and supply in the product concerned. Here, the TRSC linked market-effect factors to the concept of adverse effect, which raised the threshold for challengeability later incorporated by the *SCM Agreement*.

TRSC Art. 11:3 ruled that subsidies could be provided to give advantage to certain enterprises. The Agreement enumerated¹⁴⁴ the possible forms of subsidies. Later, the *SCM Agreement* established the principle of specificity as a requirement for the challengeability of subsidies that were not contingent upon export performance or upon the use of domestic over imported goods. The *SCM Agreement* narrowed the possibility of subsidization given to certain

¹⁴⁴ TRSC Art. 11:3.

Signatories recognize that the objectives mentioned in paragraph 1 above may be achieved, *inter alia*, by means of subsidies granted with the aim of giving an advantage to certain enterprises. Examples of possible forms of such subsidies are: government financing of commercial enterprises, including grants, loans or guarantees; government provision or government financed provision of utility, supply distribution and other operational or support services or facilities; government financing of research and development programmes; fiscal incentives; and government subscription to, or provision of, equity capital.

enterprises established under the TRSC that had a generous subsidy policy towards certain companies because of paragraph 3 of Art.11.

The TRSC Art. 11:4 established that nothing in the list enumerating domestic subsidies created any basis, in itself, for action under the *GATT 1947*. This means that the code presented a list of domestic subsidies that, according to its own definition, “may cause or threaten to cause injury,” but limited possible challengeability through the very careful language of paragraph 4, which targeted diminishing possible challenges to the enumerated subsidies of Art. 11. This article is proof that the provisions of the TRSC did not evolve from the *GATT 1947* substantive provisions and diminished the possibilities of challengeability of domestic subsidies.

The TRSC adopted an annex, entitled the “Illustrative List of Exporter Subsidies,” which listed a series of practices. The original document had been the result of a 1960 GATT process of a working-party’s negotiations.¹⁴⁵ Later, a schedule of export subsidies was established to measure the level of export subsidies of each Member under the *SCM Agreement*.

The TRSC represented an attempt to evolve from the previous *GATT 1947* regulations on agricultural subsidies. It did so regarding procedural rules of countervailing duties and dispute settlement. However, the substantive provisions, either on export or domestic agricultural subsidies, were not significantly modified. There were clarifications of specific definitions, such as “more than an equitable share,” “adverse effects,” “injury” and “serious prejudice,” used later under the *SCM Agreement* and the *AoA*. However, these modifications brought about by the TRSC had a very high cost and consequences in WTO law. They actually raised the thresholds to challenge subsidies in general and also agricultural subsidies, as the *EC – Sugar Exports* cases demonstrated. Other *GATT* cases that will be analyzed next that challenged agricultural subsidies

¹⁴⁵ GATT, *Report adopted*, GATT reprinted, 9th Supp. B.I.S.D. (1986) 185.

under the TRSC will corroborate that. It became difficult to challenge agricultural subsidies under the TRSC because of the higher thresholds of challengeability.

I.3.1.1 The *EEC – Wheat Flour Subsidies* Case and the Wrong Application of New Concepts in the TRSC, Such as “Price Undercutting”

In *European Economic Community – Subsidies on Export of Wheat Flour [EEC – Wheat Flour Subsidies]* the panel decided that it was not in position to declare that European agricultural subsidies had given to the EEC¹⁴⁶ “more than an equitable share of world export trade.” One of the reasons the panel could not condemn European agricultural subsidization under the TRSC provisions was because the code established market-effect requirements (especially price undercutting as a requirement to prove displacement) for agricultural subsidies’ challengeability that were not present in the *GATT 1947*. The new provisions of the TRSC not only established higher thresholds of challengeability, but they also could not be effectively applied by the panels, as the analysis of this case will testify.

The panel held that it could identify artificial levels of trade in the wheat flour market and made findings stating that the EEC export refunds for wheat had to be considered as a “form of subsidy” that harmed the US, even though it could not prove that EEC subsidization was not consistent with TRSC Art. 10. It is relevant to mention that subsidies were condemned under *GATT 1947* Art. XVI, even with the simpler rules with no market-effect requirements for challengeability.

¹⁴⁶ This dissertation will sometimes refer to the current European Union [EU] as European Economic Community [EEC] or European Community [EC] according to the reference of each GATT or WTO case. The European Economic Community also dubbed the European Community was an international organization that existed between 1958 and 1993 on the early stages of the European Union. When the EU was created in 1993, the EEC was transformed into the EC, one of the EU’s three pillars. Doreen Collins, *The European Economic Community*, (London: M. Robertson, 1975).

The terms of reference of the case were established in January 1982. The hearings were held in February, March and April. The panelists took one year to write the report, and the final text was circulated on March 21, 1983. The quantity of market and factual data submitted by the parties and the difficulty for the panelists to reach a decision were also factors that contributed to the delay.

The US stated that the EEC's market share had increased from 18% to 62% of the world market¹⁴⁷ because of the EEC farm subsidies. Accordingly, they alleged that this increase in market share was evidence that the export subsidy was causing the EEC to take more than an equitable share of world trade in the wheat flour market. Furthermore, the US believed that the levels of subsidization in this case were even higher than those in the Brazilian and Australian complaints.

Since the implementation of the Common Agricultural Policy for wheat in the EEC in 1960, the EEC's share of the world market in wheat flour had gone up steadily. On the other hand, during the same period, the market share of the US and other wheat flour exporters plunged. The US calculated that the EEC's share of world commercial exports of wheat flour rose from 29% to 75% in the years that preceded the complaint (1978-1979 to 1980-1981).¹⁴⁸

This scenario seemed to fit the definition that the EEC had achieved "more than an equitable share of the world export trade" in wheat flour because of the concept of "displacement" implemented in TRSC Article 10:2(a), which states:

- (a) more than an equitable share of world export trade" shall include any case in which the effect of an export subsidy granted by a signatory is to displace the

¹⁴⁷ *EEC – Wheat Flour Subsidies supra* note 54 at 7.

¹⁴⁸ "During the early 1960's, the United States had supplied 92 per cent of Saudi flour import needs while the EEC had accounted for only 2 per cent. However, during the most recent 3-year period, the US share had fallen to 38 per cent while the EEC share had risen to 61 per cent" *Ibid* at 13.

exports of another signatory bearing in mind developments in world markets.¹⁴⁹

The data was strong evidence that EEC subsidies were displacing exports from other competitors in the international wheat market. The US also proved that its products had been replaced by EEC sales in several markets and that there was evidence that price undercutting had occurred as a consequence of European subsidies. The US also alleged that price undercutting caused by the European subsidies was violating TRSC Art. 10:3, which prohibited the use of export subsidies to export primary products at “prices materially below those of other suppliers to the same market.”¹⁵⁰

The European Economic Community challenged the US complaint on several grounds. It stated that the US had highly subsidized its crops with artificial incentives as well. More importantly, it alleged that the US could not use the Tokyo Round Subsidies Code to legally challenge the EEC Common Agricultural Policy by referring to events that had occurred before the code had been adopted.¹⁵¹

The EEC also reasoned that wheat and wheat flour were the same product, and for this reason, the comparison of market shares should be made for the two products together. Their strategy was that such a comparison would show a much smaller change in market share.¹⁵²

The EEC brought forward a complex range of reasons to explain why its exports were not responsible for the US’s sales losses. Their rationale was to avoid the link of cause and effect between the US’s losses and the EEC’s market share increase. The link of cause and effect was

¹⁴⁹ See TRSC Art. 10:2.

¹⁵⁰ See TRSC Art. 10:3.

¹⁵¹ The terms of reference of the case were:

To examine, in the light of the relevant provisions of the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the *General Agreement on Tariffs and Trade* the facts of the matter referred to the Committee by the United States concerning subsidies maintained by the European Communities on the export of wheat flour and in the light of such facts to present to the Committee its finding as provided for in Article 18 of the Agreement. *EEC – Wheat Flour Subsidies supra* note at 54.

¹⁵² *Ibid* at 33 n. 2.

first applied in TRSC Art. 2.1. as one of the requirements for countervailing duty and was not present in the *GATT 1947*, either in Art. VI or XVI. It is interesting to note that this concept introduced by the countervailing duties provisions of the TRSC was used by the EEC in this case to successfully avoid challengeability of their agricultural subsidies.

The EEC also alleged that the reasons for the US's losses were unclear. They suggested that the US share of the market of wheat flour could have been affected by several economic and also non-economic factors, such as US political embargoes,¹⁵³ inability or unwillingness of US flour mills to meet demand in certain years, lack of regular transportation links, preference for EEC linguistic and cultural ties and preference for EEC flour, among others.¹⁵⁴ In this case, the EEC used the same strategy used in the other GATT cases analyzed. They could not deny or prove that they were not subsidizing; therefore, they alleged that other external factors could be interfering in the international prices and in the shares of the wheat market. Because some of these factors were subjective and others depended on econometric calculations to be proved, the panel had difficulty in identifying the real factors that interfered in the international market of the challenged product.

Furthermore, the EEC stated that it would be a complex task to economically determine what the EEC share of the wheat market in a hypothetical world market, free of agricultural subsidies, would be. The EEC alleged that the complainant could not state precisely how their subsidies had affected the potential US decline in sales, market share, profits, productivity, return on investments and other market factors. The causal link between market effect factors and

¹⁵³ *Ibid.* at 31.

¹⁵⁴ *Ibid.* at 16.

harmful effects or displacement was only possible to be proved with complex econometric calculations, as the *US – Upland Cotton*¹⁵⁵ case proved later.

The legal arguments and counter-arguments of the parties proved that, in this case, there was no agreement on the meaning of the “more than an equitable share of the world export trade” concept. Neither party agreed with the standard definition of the term used in previous *GATT 1947* cases concerning Article XVI, which was the international market share any country would have in the absence of all distortions in the world market.¹⁵⁶ This happened because the TRSC introduced new thresholds for challengeability for this concept of “more than equitable share.”

To move forward with the negotiations, the parties conceded on the definition of “equitable share” negotiated during the TRSC. However, when the definition was used to challenge the European practices, the consensus was broken. The EEC was reading “equitable share” as a term that made export subsidies possible, whereas the US was using a more specific definition, that of any increase in market share that could be causally tied to a particular export subsidy.¹⁵⁷ The arguments by both parties illustrate the complexity of the case. Both parties questioned *GATT 1947* terms such as “market share” and “displacement,” applied by the TRSC.

The panel found that EEC export refunds for wheat had to be considered as a “form of subsidy,” subject to *GATT 1947* Article XVI, and that it was evident that the EEC share of world exports of wheat flour “had increased considerably when application of EEC export subsidies was the general practice, while the share of the US and other suppliers has decreased.” Despite this, the panel was unable to conclude as to whether the increased share had resulted in the EEC’s having “more than an equitable share” in terms of Article 10. The panel could not apply

¹⁵⁵ *US – Upland Cotton AB Report supra* note 14.

¹⁵⁶ *EC – Sugar Exports (Australia) supra* note 54 and *France – Wheat Exports supra* note 57.

¹⁵⁷ *EEC – Wheat Flour Subsidies supra* note 54 at 2.

the new definitions of the TRSC and could not reach a conclusion on the main aspects of the case.

The panel could identify that there were artificial levels of trade in wheat flour, but the complexity of the market and also the new definitions in terms of market-effects made it significantly more complicated to assess the “difficulties inherent in the concept of more than an equitable share.” It also found that, despite the considerable increase in EEC exports, “market displacement in the sense of Article 10:2(a) was not evident in the seventeen markets examined by the Panel.”¹⁵⁸ In this case, the panel applied the same concept of “equitable share” used in the *EC – Sugar Exports*, trying to prove displacement based on specific markets and not on the “whole export trade market.” This approach obliged the panel to try to verify displacement in 17 different markets, which was significantly complex.

Furthermore, Professor Trebilcock analyzed *EEC – Wheat Flour Subsidies* and stated that shifts in the market share were not sufficient to prove displacement, and the panel could not determine which factors had contributed to changes in the market shares. In his opinion, the panel was looking for evidence of price undercutting to prove displacement,¹⁵⁹ so that it could be demonstrated that the EEC was getting “more than an equitable share of the world export trade” in wheat flour. Price undercutting was a concept adopted by the TRSC as a requirement to prove injury. Later, the *SCM Agreement* applied the concept as a requirement to prove injury and also serious prejudice, in the sense of Art. 5(c). *SCM Agreement* Art. 6.3 defined possible effects of

¹⁵⁸ *Ibid.* at 36.

¹⁵⁹ The Panel noted the difficult in determining whether, in fact, changes in market share could be attributable to a particular export subsidy, as opposed to other factors. It seemed to be suggesting that specific evidence of price undercutting in the market in question would be required to establish that export subsidies were unambiguously resulting in displacement – shifts in market share alone were insufficient, however dramatic. See Trebilcock, *The Regulation of Trade supra* note 29.

serious prejudice that should be taken into account for challengeability: price undercutting, displacement and increase in world market share.

We can conclude that the TRSC did not establish price undercutting as a requirement to prove displacement, as the panel seemed to interpret. Both were established as conditions to prove serious prejudice. Displacement was a variable that involved a transfer in relative shares of the market from the non-subsidizing Member to the subsidizing Member.¹⁶⁰ Differently put, price undercutting was a concept that could be proved by export unit value, comparing prices of the subsidized products with prices of non-subsidized like products in the same market.¹⁶¹

Displacement was related with the quantity of the products that built market share and price undercutting of the price of these products: two different economic variables that excluded the possibility of one's being a requirement to prove the other. Therefore, the TRSC brought in new economic variables that could not be properly applied in the cases because of their economic complexity, which made it more difficult to challenge agricultural subsidies.

Even so, the panel did hold that it was not convinced that EEC export subsidies had not caused undue disturbance to the normal commercial interests of the US in the sense of *GATT 1947* Art. XVI:2, "to the extent that it may well have resulted in reduced sales opportunities of the United States"; however, it was not enough to condemn the European subsidies for purposes of American compensation and retaliation.

The panel stated that the EEC had to make greater efforts to limit the use of subsidies on the exports of wheat flour. Furthermore, it found "anomalous" the fact that the EEC would not be able to export substantial quantities of wheat flour and increase its share in the world market, had

¹⁶⁰ See *SCM Agreement* Art. 6.4.

¹⁶¹ See *SCM Agreement* Art. 6.5.

it not subsidized its wheat production. Interestingly, the panel¹⁶² was saying that the EEC had subsidized its wheat crops; these subsidies had harmed the US, but they were not in a position to condemn the EEC's agricultural subsidies on wheat.

Lastly, the panel suggested that a clearer definition of the concept "more than equitable share" was needed, even though the TRSC had already provided it, which meant that the provisions of the Subsidies Code were not clearer than the *GATT 1947*, but were more complex. The reform of the TRSC made challengeability more difficult, as the analysis of the next case will corroborate.

I.3.1.2 The *EEC – Pasta Subsidies* Case and the Concept of "Primary Product"

In *European Economic Community – Subsidies on Export of Pasta Products* [*EEC – Pasta Subsidies*] the respondent alleged that the TRSC was not clear, and again, the panel refused to declare that the EEC had gained more than an equitable share of the world export trade in pasta because of its subsidies, despite a determination that the EEC subsidies on exports of pasta products were granted in a manner inconsistent with TRSC Art. 9. The case helps to elucidate the concept of primary products because of a dissenting opinion that held that governments had generally presumed that subsidies on primary components of non-primary products would not be prohibited by Article 9.

¹⁶² At the first meeting after the panel report, held in April 1983, the United States stated that the panel had failed to complete its task and required a plenary meeting of Subsidies Code signatories, calling upon the process of voting to find and confirm that the E.U. subsidy had taken more than an equitable share of world trade. The Community opposed the motion and asked for the report to be adopted. Each side had influence with other country parties, and both received substantial support from other countries. The debate went on for two more meetings, with no resolution. Neither party wanted to give away. The impasse went on through the 1980s, despite periodic efforts to secure adoption of the panel report. GATT, Committee on Subsidies and Countervailing Measures, *Minutes of the Meeting held on 22 April 1983*, GATT *SCM Agreement/M/14* (1983) online: WTO <http://www.wto.org/gatt_docs/English/SULPDF/91020150.pdf>.

In December 1981, two months after formally initiating a dispute settlement proceeding in the *EEC – Wheat Flour Subsidies* case, the US filed a bilateral request to the EEC, asking for consultations on another export subsidy practice – the export subsidization of pasta.¹⁶³ The US's main claim was that European subsidies on pasta violated TRSC Subsidy Code Art. 9, which explicitly prohibited all export subsidies on products other than certain primary products. The US also stated that, even if the EEC were allowed to equalize support prices with world prices, the European subsidy was overcompensating by paying more than the difference.

The EEC alleged that it was subsidizing primary product inputs into pasta production, in particular European durum wheat, which would mean subsidies on primary products allowed by the TRSC. The effect of the subsidy, according to the EEC, was simply to compensate their pasta exporters for the higher price of EEC flour compared with world prices, thereby allowing them to be competitive in the world market.

In June 1982, it was agreed that a five-Member panel would hear the case, and both parties presented their arguments. The report with the decision was not circulated until May 1983. Once again, the panel had taken a long time to reach a decision. In the final report, the majority ruled in favour of the US, while one Member filed a dissenting opinion in favour of the EEC's position. The allegation of the dissenting opinion was that governments had presumed that subsidies for primary components of non-primary products were not prohibited by TRSC Article 9.

The main legal topic in the case was the concept of “primary product” under the reform of *GATT 1947* Art. XVI in 1955 and under the TRSC. As was previously analyzed, *GATT 1947*

¹⁶³ *European Economic Community – Subsidies on Exports of Pasta Products* (1983), GATT Doc. *SCM Agreement/43*, unadopted [*EEC – Pasta Subsidies*].

Art. XVI:4¹⁶⁴ contained a flat prohibition on export subsidies for all “non-primary” products. For all “primary” products, the equitable share test of Art. XVI:3¹⁶⁵ applied. Export subsidies for pasta (if considered a non-primary product) were totally prohibited under Article XVI:3, because they were a processed form of agricultural raw materials. The parties’ opinion diverged on the definition of “primary product,” especially because, if pasta were not considered a non-primary product, subsidies would be justified under *GATT 1947* Art. XVI.

There was a statement in *GATT 1947* Annex I in Ad Article XVI that defined the primary product as “any product of farm, forest or fishery, or any mineral, in its natural form or which has undergone such processing as is customarily required to prepare it for marketing in substantial volume in international trade.”¹⁶⁶ The Committee on Trade on Agriculture also addressed the question of what constituted primary products. Because the definition was not crystal clear, the committee suggested that *GATT 1947* Members could establish a list of products that constituted a primary product. The TRSC provided an illustrative list of prohibited export subsidies on manufactured products, but not on agricultural products, which demonstrated the difficulties involved in reaching a definition.

¹⁶⁴ *GATT 1947* Article. XVI.4.

Further, as from 1 January 1958 or the earliest practicable date thereafter, contracting parties shall cease to grant either directly or indirectly any form of subsidy on the export of any product other than a primary product which subsidy results in the sale of such product for export at a price lower than the comparable price charged for the like product to buyers in the domestic market. Until 31 December 1957 no contracting party shall extend the scope of any such subsidization beyond that existing on 1 January 1955 by the introduction of new, or the extension of existing, subsidies.

¹⁶⁵ *GATT 1947* Article. XVI.3.

Accordingly, contracting parties should seek to avoid the use of subsidies on the export of primary products. If, however, a contracting party grants directly or indirectly any form of subsidy which operates to increase the export of any primary product from its territory, such subsidy shall not be applied in a manner which results in that contracting party having more than an equitable share of world export trade in that product, account being taken of the shares of the contracting parties in such trade in the product during a previous representative period, and any special factors which may have affected or may be affecting such trade in the product.

¹⁶⁶ See *supra* note 64.

Regarding subsidization of the primary product component of a processed product, *GATT 1947* Art. XVI:4 and TRSC Art. 9 clearly prohibited export subsidies on processed products. In this case, the problem was not the rule, but ancient practices of agricultural subsidization that had not been challenged in the past. Because agricultural export subsidies were allowed to a certain extent in *GATT 1947* Art. XVI:3 and export subsidies for manufactured products were prohibited in Art. XVI:4, it was difficult to know at what stage the subsidization of processed agricultural products should stop. It was also difficult to establish a clear line on whether the processed product that was a non-primary product should escape from the rules of Article XVI:3, as this case demonstrated.

There was a view that agreed with the prohibition of subsidization of a primary product component of an exported processed product because it was under the regulation of *GATT 1947* Art. XVI:4 and TRSC Art. 9. Another view agreed that this sort of subsidization should be authorized to the extent that it did not give to the subsidizing Member more than an equitable share of the world trade export of that product, because it had to be considered as an export primary subsidy under the regulation of *GATT 1947* Art. XVI:3. The committee suggested that there could be a rule that the subsidy granted on the processed product be no higher than the equivalent of that on the primary product component.¹⁶⁷

At any rate, the panel concluded that “neither party had finally contended that pasta was a primary product” and thus determined that “pasta was a processed product.”¹⁶⁸ The panel read Article 9 literally to include all subsidies given to exporters of non-primary products, which included subsidies indirectly paid to a primary product.

¹⁶⁷ “Reference was made by analogy to what existed under rules of origin, wherein the added value determined the origin of the product, as well as to the drawback system which permitted the refund at exportation of the duty paid on the imported content of a manufactured product.” *GATT CTA Report supra* note 51 at para 68.

¹⁶⁸ *EEC – Pasta Subsidies supra* note 163 at 9-10 para. 4.2.

The EEC's response to the panel was that, even though pasta could be considered a "non-primary agricultural product," the TRSC was unclear as to whether this was in fact the case, and therefore, the question concerning pasta's status as a primary or non-primary agricultural product should be resolved by negotiation rather than by the *GATT 1947* dispute settlement system. Moreover, the EEC developed a legal theory and stated that "export subsidies on processed products were permissible to the extent they related to any primary products which they contained."¹⁶⁹

The majority of the panel rejected this European reasoning; however, the allegation that the TRSC was unclear was a strong argument, because parties did not agree on the concepts established in the code, especially on Art. 10, which regulated agricultural export subsidies.

At the time that *GATT 1947* Art. XVI:3 was being adopted,¹⁷⁰ the US had announced a reservation. The country continued to grant export subsidies on raw cotton to equalize the high cost of cotton created by US support prices. This also was the reason that the EEC gave for its subsidizing of pasta,¹⁷¹ to equalize costs. According to the US, the country was subsidizing cotton because of the old US *GATT 1947* reservation. Therefore, because neither the EEC nor any other signatory had entered similar reservation to the new code, the EEC had no basis for making an exception. The EEC argued that, if the subsidy on pasta's wheat flour was not a subsidy on a "non-primary" product, it, at least, had to be considered as a "primary" product subsidy. If this were true, the US, then, would have to prove that the EEC had gained "more than an equitable share" of the world wheat flour markets.¹⁷²

¹⁶⁹ Edmond McGovern, *International Trade Regulation. GATT, the United States and the European Community*, 2nd ed. (Exeter: Globefield Press., 1983) at.329 cited in A. Swinbank "The EU's Export Refunds on Processed Foods: Legitimate in the WTO?" (2006) 7 *The Estey Centre Journal of International Law and Trade Policy* 152 at 155.

¹⁷⁰ As previously stated, in 1955, the GATT had added new provisions to Article XVI on subsidies.

¹⁷¹ *EEC – Pasta Subsidies supra* note 163 at 4 paras. 2-13 to 12-17.

¹⁷² *Ibid.* at para. 3.6.

The EEC alleged that the TRSC had been understood to allow all types of export subsidies on raw materials. For this reason, there was a kind of “universal understanding” of its meaning that had to be accepted by *GATT 1947* contracting parties. This argument was supported by several other governments that were also subsidizing raw material for exports. The EEC also stated that the US had not alleged that it had been injured by the European subsidies. Furthermore, the EEC stated that durum wheat was a primary product, within the meaning of the *GATT 1947* Art. XVI:3, as well as one of the primary products referred to in the TRSC Art. 10. According to these provisions, exports of products from this category could be subsidized on the condition that the principle of “equitable share of the world trade” was respected. The EEC alleged there was no other restriction for a primary product’s subsidization and that there was no doubt that durum wheat was a primary product.¹⁷³

The panel upheld the definition of “certain primary products” in Art. 9 of the TRSC, footnote 29,¹⁷⁴ and, as such, primary products included only a product of farm, forest or fishery in its natural form or one that had been processed in preparation for marketing in international trade. The panel found that EEC exports refunds were granted on the export of pasta and that it did increase exports of pasta products by refunding a part of the cost of these processed products.¹⁷⁵

The panel also found that the US’s reservation about *GATT 1947* Art. XVI:4 was not relevant to the US’s position under the TRSC, since it was a different legal arena. The panelists held that it was not necessary to reach a conclusion on the question of a possible “absence of any allegation by the United States in respect of injury.” The concept of injury was not a requirement

¹⁷³ *Ibid.* at 8 para. 3.11.

¹⁷⁴ TRSC n. 29 “For purposes of this Agreement “certain primary products” means the products referred to in Note Ad Article XVI of the General Agreement, Section B, paragraph 2, with the deletion of the words “or any mineral”.

¹⁷⁵ *EEC – Pasta Subsidies supra* note 163 at 10 para. 4.4.

for challengeability of agricultural subsidies under TRSC Art. 10. According to the panel, there was a presumption that injury¹⁷⁶ happened in a case like this. Furthermore, the EEC had a reasonable opportunity to rebut this presumption.

Finally, the panel held that the EEC subsidies on exports of pasta products were granted “in a manner inconsistent with Article 9 of the Code.”¹⁷⁷ Once again, a decision under the TRSC identified strong evidence of illegal agricultural subsidization, but condemnation was not possible because the panel could not prove that the EEC’s support on pasta had given it “more than an equitable share of world export trade” in this product.

The EEC blocked adoption of the report¹⁷⁸ because of the dissenting opinion filed by one of the panel Members. The EEC interpreted the dissension as being permission for governments to be guided by whichever opinion they wanted.

The *EEC – Pasta Subsidies* was settled in August 1987, after an interim agreement in 1986¹⁷⁹ in which the US accepted¹⁸⁰ the EEC’s export subsidies for raw materials, with the

¹⁷⁶ Later the *SCM Agreement* linked the concept of injury to countervailing duties and the adverse effect caused by export agricultural subsidies could either nullify or impair any benefit previously given under any WTO Agreement or could cause serious prejudice, which was the case of the *EEC – Pasta Subsidies supra* note 163.

¹⁷⁷ *Ibid.* at 12 para. 4-14.

¹⁷⁸ The result was another deadlock similar to the one in the *EEC - Wheat Flour Subsidies supra* note 47, that was going on at the same time. However, unlike *EEC - Wheat Flour Subsidies*, the *EEC – Pasta Subsidies* was, from one way or another, settled. Actually, the U.S began to retaliate against the EC, raising tariffs for EC imports of pasta in November 1985 because the EC was not complying with another panel decision in the *Citrus* case. The EC counter-retaliated raising tariffs on US lemons and walnuts. See Finger, Michael & Fung K. “Can Competition Policy control 301?” *World Bank Policy Research Paper Series 1253, 1994* (Washington D.C.: The World Bank. Policy Research Department. Trade Policy Division, 1994).

¹⁷⁹ The theory of the settlement is written into the Dunkel draft of the Uruguay Round *Agreement on Agriculture*. See AoA Art. 11, cited in GATT, Trade Negotiations Committee, *Meeting of 5-7 February 1992*, GATT MTN.TNC/W/FA, online: WTO http://www.wto.org/gatt_docs/English/SULPDF/92130126.pdf.

¹⁸⁰ In practical terms, the United States, agreed that 50 percent of its pasta exports to the United States would be produced under inward processing relief (IPR) arrangements (under which the raw material would be imported into the EU free of import duty, and the resulting pasta exported without export subsidy), and that the export subsidy on the remaining exports to the United States would be reduced by 27.5 percent. Even though the US did not succeed in eliminating the subsidy itself, it prevailed on the claim that asked to abolish over compensation (price difference in the international and national market). EC, *The Agricultural Situation in the Community 1987 Report* (Luxembourg: Office for Official Publications of the European Communities, 1988) at 113.

stipulation that the subsidy was not to be greater than the actual difference between domestic and world market prices.¹⁸¹

It can be concluded that the panels of the two cases on agricultural subsidies brought under TRSC Art. 10 could not condemn illegal subsidizing practices, while the panels under the *GATT 1947* were clear in condemning agricultural subsidization under Art. XVI. This corroborates the conclusion that the TRSC brought about some legislative advances in terms of procedural rules, but not in terms of challengeability for agricultural subsidies. The panels had difficulty in applying the new concept of the TRSC and, sometimes, applied it incorrectly.

One could state that the difficulties with the TRSC procedural provisions were because it was a new agreement and the signatories were not used to its regulation, however, the signatories negotiated it. Therefore, the most plausible conclusion is that the TRSC procedural provisions were difficult to be applied because they were ambiguous and imposed higher thresholds of challengeability. Even though the causal link of these conclusions cannot be proved, they are consistent with the hypothesis that market effects included in the TRSC could not be properly identified and analyzed by the panels.

I.4 Other Possibilities for Challengeability for Agricultural Subsidies under the *GATT 1947*

Challengeability under *GATT 1947* Art. XVI has been analyzed. However, during the *GATT 1947* years, agricultural subsidies could also be challenged under Art. VI (countervailing duties) and Art. XXIII 1(b) (nullification or impairment) either because of Art. II (schedules of concessions) or Art. III (national treatment). Because the Peace Clause also limited

¹⁸¹ The settlement on pasta is recorded in EC, [1987] Official Journal (O.J.) L 275/36.

challengeability under these articles, the following section will analyze its rules to compare them with the rules established after the Peace Clause.

I.4.1 Countervailing Duties—*GATT 1947* Art. VI and TRSC Regulation

Prior to analyzing *GATT 1947* Art. VI it is relevant to mention that countervailing duties, anti-dumping measures and safeguard measures are domestic trade remedies. A countervailing duty is the remedy that an importer state can use against subsidies given in the exporter state. The regulation of trade remedies under the WTO is a different obligation. In this case, the WTO rules only give legal guidance for the national application of these remedies on the country of the imported goods. However, the exporting country still can challenge any of these trade remedies in the WTO dispute settlement system. This dissertation also analyzes countervailing duties because *AoA* Art. 13 also limited subsidies' challengeability through countervailing duties.

GATT 1947 Art. VI set up the rules for countervailing agricultural and non-agricultural subsidies. Later, the TRSC implemented procedural rules to clarify and systematize the *GATT 1947* regulation of countervailing duties. The regulation became more complex because of the introduction of market-effect requirements for subsidies' challengeability, especially in the definition of "material injury." This meant a higher threshold to challenge subsidies than previously required by the *GATT 1947*.

GATT 1947 Art. VI paragraph 3 established that no countervailing duty should be applied in excess of the amount of subsidy granted. Paragraph 5 established that no product could be subject to both anti-dumping and countervailing duties as compensation for the same situation of dumping or export subsidization.

Paragraph 6 set parameters for challengeability. Part “a” stated that countervailing duties could only be applied if the effect of the subsidization were to cause or threaten material injury to a domestic industry or even to postpone the establishment of a domestic industry. Part b established that contracting parties could waive the requirements of Part “a” (cause or threaten material injury to a domestic industry) to permit a contracting party to levy an antidumping or countervailing duty on the import of any product if such import caused or threatened material injury to an industry of another contracting party that exported the product concerned to the importing country.¹⁸²

In this provision, the *GATT 1947* allowed an importing country to countervail a subsidy that was harming a third country that exported a like product. This was a surprising *GATT 1947* provision, allowing importing countries to apply countervailing duties on imports that were displacing exports of third countries, if injury could be proved. The concept of applying countervailing duties on the importation of subsidized products harming a third country was implemented neither in the TRSC nor in the *SCM Agreement*. The *GATT 1947* had a form of challengeability for subsidies that was not established in the later agreements that regulated subsidies, which proves the level of sophistication of the *GATT 1947* in terms of challengeability when compared with its successor agreements.

We could say that this provision was not implemented by later subsidy agreements because of its high level of complexity or because it was difficult to implement. If this rationale were correct, the Agreement on Implementation of Article VI of the *General Agreement on Tariffs and Trade* 1994 [The Antidumping Agreement]¹⁸³ would not have implemented a very similar provision. Article 14 of the Antidumping Agreement, called “Anti-Dumping Action on

¹⁸² See GATT Art. VI (b).

¹⁸³ *Agreement on Implementation of Article VI of the General Agreement on Tariffs and Trade* 1994 [The Antidumping Agreement]. *WTO Legal Texts supra* note 1.

Behalf of a Third Country,” established that anti-dumping on behalf of a third country could be applied under certain conditions.¹⁸⁴

Therefore, *GATT 1947* proved once again that its simple and more generic provisions made the challengeability of subsidies possible in some cases that not even the more complex and elaborate provisions of the TRSC and the *SCM Agreement* made possible. One example was the provision of *GATT 1947* VI:6 (b), because it had no parallel in either the TRSC or the *SCM Agreement*.

Paragraph (c) of *GATT 1947* Art. 3 established that a countervailing duty could only be levied if the other *GATT 1947* contracting parties approved it. If there were a delay that could cause damage difficult to repair, the importing contracting party could levy a countervailing duty without the approval of the other contracting parties.¹⁸⁵

Paragraph 7 established a different treatment for subsidies on primary commodities that resulted in the sale of the commodity for export at a price lower than the comparable price charged for the like product in the domestic market. It stated that, in this case, there was no presumption of material injury if there was consultation among the interested contracting parties and the subsidies also resulted in the sale of the commodity at a higher price than that charged for the like product and did not unduly stimulate exports.¹⁸⁶ Paragraph 7 did not even mention

¹⁸⁴ Anti-Dumping Agreement Art. 14 establishes:

An application for anti-dumping action on behalf of a third country shall be made by the authorities of the third country requesting action. 14.2 Such an application shall be supported by price information to show that the imports are being dumped and by detailed information to show that the alleged dumping is causing injury to the domestic industry concerned in the third country... In considering such an application, the authorities of the importing country shall consider the effects of the alleged dumping on the industry concerned as a whole in the third country... The decision whether or not to proceed with a case shall rest with the importing country.

¹⁸⁵ *GATT* Art. VI: 6(c):

In exceptional circumstance, however, where delay might cause damage which would be difficult to repair, a contracting party may levy a countervailing duty for the purpose referred to in subparagraph (b) of this paragraph without the prior approval of the CONTRACTING PARTIES and that the countervailing duty shall be withdrawn promptly if the CONTRACTING PARTIES disapprove.

¹⁸⁶ See *GATT* Art. VI 7 (a) and (b).

the word “subsidies”; it referred to “a system for the stabilization of the domestic price or of the return to domestic producers of a primary commodity.” The main goal of this paragraph was to state that there was no presumption of material injury if a primary commodity was exported at a cheaper price than it cost in the national market. We could say that it established a different treatment for agricultural subsidization, since there was no such provision for non-primary products. However, there was no *GATT 1947* case on countervailing subsidies under this provision.

It is relevant to note that in Annex I of *GATT 1947* “Notes and Supplementary Provisions” Ad Article XVI to paragraph 3 of the *GATT 1947* had almost the same wording as paragraph 7 of Art. VI. Art. XVI to paragraph 3 stated that export subsidies on primary products that “results in the sale of the product for export at a price lower than the comparable price charged for the like product to buyers in the domestic market, shall be considered not to involve a subsidy on exports.” The conditions were two: a) *GATT 1947* Members determined that the export subsidy also resulted in the sale of the product at a higher price than the comparable price charged for the product in the domestic market and b) the subsidy did not unduly foster exports that caused prejudice to other *GATT 1947* Members.

The result was that neither the material injury referred to in paragraph 7 of Art. VI nor export subsidies regulated in Ad Art. XVI could be presumed for primary products, even if the agricultural product was exported at a cheaper price than it was sold for in the domestic market. There was a prohibition in *GATT 1947* Art. XVI:4 on export subsidization of non-primary products that resulted in the sale of this product at a lower price than the one charged for the like product in the domestic market. The prohibition did not include primary products; therefore, the reason for the existence of Ad Art. XVI to paragraph 3 was to emphasize that export

subsidization of primary products was allowed under the *GATT 1947*, even when export prices were lower than domestic prices for the subsidized product – if they did not give the exporting Member more than an equitable share of the world export trade in that product.

During the *GATT 1947* years, export subsidies were prohibited if they gave the subsidizing Member “more than an equitable share of the world export trade” in the subsidized product. In this sense, the fact that the subsidized product was sold at a lower price in the domestic market than in the international market after being exported was not relevant. During the *GATT 1947* period, there was no prohibition on export subsidies of primary products, but there was a limitation set on this sort of subsidy if it gave the subsidizing Member “more than an equitable share.” This means that export subsidies under the *GATT 1947* had to displace the exports of other Members and consequently had to cause these Members harm in order to be limited.

The fact that a product is sold at a cheaper price in the domestic market than on the international market is strong evidence of subsidization. It is very unlikely that a product with no subsidy would be cheaper after all the export costs, such as transportation, insurance and freight. However, it is possible that a subsidized product sold at a lower price in the domestic market than in the international market did not have harmful effects on another Member. That is the reason for the existence of *GATT 1947* Ad Art. XVI to paragraph 3.

The TRSC brought in several procedural rules in the countervailing legislation but did not change the substantive regulation of the *GATT 1947*, as has been stated in this study. It is relevant to note that, in *Brazil – Measures Affecting Desiccated Coconut* [*Brazil – Desiccated Coconut*],¹⁸⁷ the panel found that *GATT 1947* Art. VI should be applied together with the TRSC;

¹⁸⁷ *Brazil – Measures Affecting Desiccated Coconut* (1996), WTO Doc. WT/DS22/R (Panel Report), online: WTO <<http://docsonline.wto.org/gen. search/asp>> [*Brazil – Desiccated Coconut*].

otherwise Members would be subject to “a package of rights and obligations that were potentially more onerous than those to which they were subject under Article VI in conjunction with the Tokyo Round Subsidies Code when they initiated the investigation.”¹⁸⁸ This decision proves that *GATT 1947* Art. VI had more stringent rules for subsidizing signatories than did the TRSC. Consequently, it is evident that TRSC procedural rules imposed a higher threshold for the challengeability of subsidies, which made subsidization harder to be challenged.

The panel ruled that the TRSC did not only impose additional obligations on a contracting party imposing countervailing duties, but that it also added some rights for such contracting party. It made certain obligations imposed by Article VI in conjunction with either the TRSC or the *SCM Agreement* less stringent and easier to meet than obligations imposed by *GATT 1947* Article VI in isolation.¹⁸⁹

Article 1 of the TRSC established that the imposition of a countervailing duty should be levied in accordance with provisions of *GATT 1947* Art. VI. TRSC Art. 2 set up three requirements for imposing a countervailing duty: (a) subsidy, (b) injury according to the concept of *GATT 1947* Art. VI and (c) a causal link between the subsidized import and the alleged injury. The *GATT 1947* Agreement did not have the casual link as a requirement for a countervailing duty. The requirements were only (a) subsidy and (b) injury. The casual link had to be proved, but not in the systematic way created by the TRSC, which imposed a higher threshold for challenging subsidies.

Paragraph 2 established that each signatory had to notify the Committee on Subsidies and Countervailing Measures, which would verify whether there was enough evidence to initiate an investigation. If there were, a public notice had to be published and the complainants notified.

¹⁸⁸ *Ibid.* at 67.

¹⁸⁹ *Brazil – Desiccated Coconut supra* note 187 at 67 paras. 246-253.

This notice had to describe the subsidy involved and guarantee to all interested parties a reasonable opportunity to present in writing and orally justify their reasoning to the investigating authorities.¹⁹⁰ Upon initiation of an investigation, evidence of both injury and subsidy had to be considered simultaneously. Paragraphs 6 and 7 set up the procedures to deal with confidential information, and the subsequent paragraph established that investigations could take place in the territory of any signatory and also on the premises of a firm if it agreed and the signatory in question did not object. If any signatory refused access or did not provide the needed information, findings could be made on the basis of facts available.¹⁹¹

The investigation could not stop customs procedures and, according to the TRSC, the investigation could not take longer than one year.¹⁹² This period of one year was kept by the *SCM Agreement* with the addition that “in no case more than 18 months, after their initiation.”¹⁹³ Public notice should be given in any affirmative, negative, preliminary or final decision with the reasons that motivated the decision. The committee should receive a report of any countervailing duty levied under the inspection of the *GATT 1947* secretariat. The signatories also should submit a semi-annual report on any countervailing duty applied in the preceding six months.

TRSC Art. 3 established all the domestic procedures for the investigation of, determination about and decision to levy countervailing duties. The *GATT 1947* did not specify them in such a manner. The rules established by the *GATT 1947* on domestic investigation only pronounced on the amount of countervailing duty levied that could not be in excess of the subsidy granted, products subject to countervailing duty being subject to countervailing duty because of any exemption of such products from duties or taxes borne by the like product and

¹⁹⁰ See TRSC Art. 2 paragraph 3 and 4.

¹⁹¹ *Ibid.* at para. 9.

¹⁹² *Ibid.* at paras. 13 and 14.

¹⁹³ See *SCM Agreement* Art. 11:11.

material injury as the requirement for countervailing duties. There were no procedural rules under the *GATT 1947* for this specific topic.

Article 3 established rules for consultation. After a request to initiate an investigation, preferably before the initiation (though it could advance to the period of the investigation), there must be an opportunity for consultations for a possible mutually agreed solution. The TRSC did not determine a specific period of time in which consultations had to finish; it only stated that consultations should not prevent national authorities from starting and processing an investigation and reaching preliminary or final findings. Later, the *SCM Agreement* kept a similar provision and did not define a specific limit of time for consultations, either. Under the *SCM Agreement*, it was established that “the subject of investigation shall be afforded a reasonable opportunity to continue consultations.”¹⁹⁴

TRSC paragraph 4 established rules for imposing countervailing duties and clearly determined that the decision to levy them was upon national authorities. It also established, following *GATT 1947* Art. VI:3, that no countervailing duty should be imposed in excess of the amount of the subsidy investigated. Letter 3 mentioned appropriate amounts on a non-discriminatory basis, which meant that countervailing duties should be applied to imports of all subsidizing sources that caused injury.

After reasonable efforts to complete consultations, a signatory could make a final determination about the existence of a subsidy causing injury, and it could impose countervailing duties. The imposition could be suspended if the government of the exporting country agreed to limit or eliminate subsidies, the exporter agreed to revise its price and the national authority of the importing country was satisfied. The evaluation of the injury could continue, and the price undertaking could be suggested by the importing authorities but the exports was not obliged to

¹⁹⁴ See *SCM Agreement* Art. 13:2.

accept the suggested price. If the exporter accepted the undertaking suggested by the importer, either on a possible limitation of exporters or on a suggested price, the exporter might periodically be required to provide information relevant to the fulfillment of such undertaking. If the exporter failed to comply with the terms of the undertaking, application of provisional measures or definitive duties using the best information available could be applied.¹⁹⁵

Undertakings could not remain longer than a possible countervailing duty would last. At any rate, if any countervailing duty investigation was suspended upon the undertaking, it had to be officially notified and published with the conclusions and reasons justifying the suspension. Countervailing duties had to “remain in force” to the extent necessary to counteract the subsidization that was causing injury. The imposition had to be reviewed, but the TRSC did not establish a specific period of time for this revision.¹⁹⁶ Later, the *SCM Agreement* established a maximum period of five years for applying definitive countervailing duties but did not regulate a specific time for administrative reviews.¹⁹⁷ It established “judicial review” of the administrative actions relating to final determinations and review of determinations.¹⁹⁸

TRSC Art. 5 regulated provisional measures that could occur after a preliminary finding that a subsidy existed under sufficient evidence of injury.¹⁹⁹ The goal was to avoid injury being caused during the period of an investigation. Provisional measures under the TRSC were provisional countervailing duties guaranteed by cash deposits or bonds equal to the amount of the subsidies provisionally calculated.²⁰⁰ Provisional measures could not last more than four months.²⁰¹

¹⁹⁵ See TRSC Art. 4

¹⁹⁶ *Ibid.* at paras.7, 8 and 9.

¹⁹⁷ See *SCM Agreement* Art. 21.2 and 21.3.

¹⁹⁸ *Ibid.* at Art. 23.

¹⁹⁹ See TRSC Art. 2 para. 1 (a) to (c).

²⁰⁰ *Ibid.* at Art. 5:2.

²⁰¹ *Ibid.* at Art. 5:4.

Countervailing duties could be applied retroactively when a final finding of injury was determined and if any provisional measure was applied during the period of investigation.²⁰² If a final finding was negative, any deposit made during the period of application of provisional measures had to be refunded. If the definitive measure was higher than the provisional measure applied, the difference was not collected. If the definitive duty was less than the amount guaranteed, the excess was reimbursed.²⁰³ The TRSC authorized application of countervailing duties in specific cases 90 days retroactively from the date of application of the provisional measure. The *GATT 1947* did not have any provision for the application of provisional measures.

TRSC Art. 6 tried to define the meaning of the word “injury” in *GATT 1947* Art. 6 by using market-effect parameters. It was necessary to have an objective examination of a) the volume of the subsidized imports and their impact on prices in the domestic market of like products (a significant increase in the volume of subsidized imports) and b) the impact of such imports on domestic producers (price undercutting, price depression or prevention of price increases on the importing country).²⁰⁴

It is interesting to note that paragraph 2 established that no one or several of these factors could give a precise guidance to the determination of injury.²⁰⁵ The treaty was basically stating that, even though requirements to determine injury were being created, they did not necessarily provide a clear and determinant manner to identify injury. This could lead to a conclusion that the creation of procedural rules in the TRSC to determine and to “clarify” substantive concepts of the *GATT 1947* did not necessarily give “decisive guidance” about these concepts.

²⁰² *Ibid.* at Art. 5:5.

²⁰³ *Ibid.* at paras. 5 to 8.

²⁰⁴ See TRSC Art 6.1 and 6.2.

²⁰⁵ *Ibid.*

Paragraph 3 established that the impact on the domestic industry must take into account an evaluation of “all” relevant economic factors that interfered in the state of the industry of the importing country that might be harmed by subsidies of the exporting country, such as:

[A]ctual and potential decline in output, sales, market share, profits, productivity, return on investments, or utilization of capacity; factors affecting domestic prices; actual and potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investment and, in the case of agriculture, whether there has been an increased burden on Government support programmes.²⁰⁶

The TRSC imposed several market-effect factors of analysis to determine injury, which made it highly complex to determine whether a company or a specific economic sector was being harmed by subsidized imports. The TRSC established that “all” relevant economic factors that interfered in the state of an industry had to be taken into account for a determination of injury.

Evidently, it was highly difficult, especially for a legal provision, to frame all the economic factors that could interfere in the determination of a concept legally defined. That was the reason that the same paragraph established that the list of economic factors to be analyzed was not exhaustive. Consequently, paragraph 3 also stated that no one or several of these economic factors would give decisive guidance for a determination of injury. It is relevant to note that the *GATT 1947* was criticized for some not accurate definitions, such as “more than an equitable share”; however, the TRSC and later the *SCM Agreement* had the same problem with some concepts, such as “injury.” The TRSC’s concept of injury was vague, because it was not able to determine a precise definition due to the unlimited economic factors brought into the concept.

²⁰⁶ *Ibid.* at Art. 6:3.

The TRSC²⁰⁷ also regulated a system of notification of subsidies that was first mentioned in *GATT 1947* Art. XVI.²⁰⁸ Any signatory could make a written request to ask for information about given subsidies that increased exports of any product from or imports into its territory. The committee would analyze the cases where a signatory considered that such information was omitted by any other signatory.

It can be concluded by the analysis of *GATT 1947* Art. VI and TRSC provisions, that the latter, through procedural rules, tried to clarify the material provisions of the former. Normally, the TRSC quoted the provisions of the *GATT 1947* and established several provisions that were supposed to clarify and make compliance with the *GATT 1947*'s rules possible. TRSC Art. 7 was an example of this. It quoted *GATT 1947* Art. XVI's determination that any subsidizing country had to notify other signatories about its subsidies and then regulated how signatories had to notify subsidies in order to comply with *GATT 1947* Art. XVI's requirements.

The problem is that the TRSC added market-effect concepts and economic factors that could not be precisely framed and measured by a legal analysis to prove injury and to challenge subsidies – either through countervailing duties or through *GATT 1947* Art. XVI. The last statement of paragraphs 2 and 3 of TRSC Art. 6 stated that no one of the economic factors could necessarily give decisive guidance on the concept of “injury.”²⁰⁹ The result was that such an imprecise definition brought about a higher threshold for challengeability of subsidies. Market-

²⁰⁷ *Ibid.* at Art. 7.

²⁰⁸ *GATT* Art. XVI:1:

If any contracting party grants or maintains any subsidy, including any form of income or price support, which operates directly or indirectly to increase exports of any product from, or to reduce imports of any product into, its territory, it shall notify the CONTRACTING PARTIES in writing of the extent and nature of the subsidization, of the estimated effect of the subsidization on the quantity of the affected product or products imported into or exported from its territory and of the circumstances making the subsidization necessary.

²⁰⁹ TRSC Art. 6.2 states that “... [n]o one or several of these factors can necessarily give decisive guidance”. TRSC Art. 6.3 states that “...[t]his list is not exhaustive, nor can one or several of these factors necessarily give decisive guidance.”

effect rules, which had requirements for subsidies' challengeability based upon economic factors, could only be complied with through econometric calculations.

GATT 1947 Art. XXIII, which had a different threshold for challengeability that was also regulated by the TRSC, will be analyzed next, because it represented another possibility for the challengeability of agricultural subsidies that was limited by the Peace Clause.

I.4.2. Nullification or Impairment of Any Benefit—*GATT 1947* Art. XXIII

GATT 1947 Art. XXIII had a less complex threshold for subsidies' challengeability than Art. XVI, because of the market-effect requirements of "more than an equitable share of the world export trade" contemplated in Art. XVI. An agricultural subsidy could be challenged under *GATT 1947* Art. XXIII if it nullified benefits previously given to a country through tariff concessions.

The article established that contracting parties could have their directly or indirectly accrued benefits nullified or impaired under the *GATT 1947* by a) any failure of another contracting party to comply with its obligations under *GATT 1947*, b) any measure of another contracting party, whether or not it conflicted with the *GATT 1947* and c) the existence of any other situation.²¹⁰

It is relevant to mention that *GATT 1947* Article XXIII is the pillar of the WTO dispute settlement system. However, the most common use or effect of this article is regarding XXIII 1(b) – the *non-violation* claims – that is the one mentioned in the Peace Clause. Therefore, this study will focus on Art. XXIII 1(b).

²¹⁰ See *GATT* Art. XXIII:1 (a), (b) and (c).

The threshold for challengeability under this article could be a violation of commitments established in the schedules of concessions, even though this measure did not conflict with *GATT 1947* rules. Part (c) stated that any contracting party had the right to have analyzed an allegation of nullification or impairment of any benefit in any circumstance. That was a broad possibility of analysis of a violation, different from Art. XVI, which had a higher threshold of challengeability because of the market-effect requirements added by the TRSC, later incorporated by the *SCM Agreement*. It is important to note, however, that Art. XXIII 1(c) has not been used since the GATT years. Therefore, this study will focus on Art. XXIII 1(b) as previously stated.

Normally, Art. XXIII 1(b) was used to challenge a subsidy because a violation of the *GATT 1947* schedule of concessions (Art. II)²¹¹ or because the subsidy could not be properly used according to the requirements of Art. III:8 (b). Both possibilities of challengeability will be analyzed next.

I.4.2.1 *GATT 1947* Article II—Schedule of Concessions

GATT 1947 Arts. II and XXIII 1(b) had a lower threshold for subsidies' challengeability, because it did not have market-effect requirements. An agricultural subsidy could be challenged

²¹¹ *GATT* Art. XXIII could be used to challenge subsidies that had violated any *GATT* provision (Art. XXIII(a)) or to challenge subsidies that even though were no in conflict with any *GATT* provision could cause any harmful effect to any Member (Art. XXIII(b) – the non-violation provision. Petersmann explains the reasons *GATT* Art. XIII(b) was created:

The fear that Member states would circumvent binding tariff reductions made *GATT* drafters create a non-violation provision – *GATT* Article. XXIII(b). This article entitled a contracting party, even in the absence of a breach of obligation by another contracting party, to argue that their benefits had been nullified or impaired under the *GATT 1947*, authorizing the harmed country to receive compensation. Ernst-Ulrich Petersmann, “Violation-Complaints and Non-Violation Complaints in Public International Trade Law” (1991) 34 *German Y.B. Intl L.* 175 at 192.

under these provisions if it nullified benefits²¹² previously given to a country through tariff concessions.

Regarding Art. II, *GATT 1947* rounds created general and specific commitments for Members on tariff reduction aimed at trade liberalization. These specific obligations were listed in the “schedule of concessions” that determined tariff concessions and other commitments that were made in the rounds of negotiations.

On trade in goods, according to *GATT 1947* Art. II, these concessions represented maximum tariff levels, dubbed “bound tariffs” or “bindings.” In agriculture, the commitments were not only maximum tariff rates, but also tariff rate quotas and limits on export subsidies and on some domestic subsidies. All schedules of concessions of the *GATT 1947*’s Members were annexed to the Protocol of Provisional Application to the *GATT 1947* or to a Protocol of Accession.

Sometimes, a Member’s tariff concessions were not determined by only one legal vehicle or agreement. According to *GATT 1947* Article XXVIII,²¹³ the obligation of the schedules can

²¹² Petesmann describes the system of tariff concessions in the GATT:

After tariff reduction was achieved, the GATT architects established a legal mechanism in which schedules of tariff concessions were binding and their value or effect could be guaranteed with the help of various general obligations, such as those mandated by national treatment principles. In addition, procedures for dispute settlement were established, taking into account legal obligations, as just one option among various kinds of diplomatic instruments intended to maintain the tariff concessions. Ernst-Ulrich Petersmann, “The Dispute Settlement System of the World Trade Organization and the Evolution of the GATT Dispute Settlement system since 1948” (1994) 31 COMMON MKT. L. REV. 1157 at 1171.

²¹³ GATT Art. XXVIII:

On the first day of each three-year period, the first period beginning on 1 January 1958 (or on the first day of any other period that may be specified by the CONTRACTING PARTIES by two-thirds of the votes cast) a contracting party (hereinafter in this Article referred to as the “applicant contracting party”) may, by negotiation and Agreement with any contracting party with which such concession was initially negotiated and with any other contracting party determined by the CONTRACTING PARTIES to have a principal supplying interest (which two preceding categories of contracting parties, together with the applicant contracting party, are in this Article hereinafter referred to as the “contracting parties primarily concerned”), and subject to consultation with any other contracting party determined by the CONTRACTING PARTIES to have a substantial interest in such concession, modify or withdraw a concession included in the appropriate schedule annexed to this Agreement.

change over the years and suffer several modifications,²¹⁴ which could include compensatory adjustment and the contracting parties maintaining a general level of reciprocal and mutually advantageous concessions not less favorable than was established prior to such negotiations.²¹⁵

GATT 1947 Art. II established that each contracting party had to receive treatment no less favorable than that provided in the appropriate schedule annexed to the *GATT 1947*, which meant that contracting parties had to respect the schedules of concessions.²¹⁶ *GATT 1947* Art. II (b) established that the products described in Part I of the schedule were exempt from ordinary customs duties in excess of what had been established in the schedules.²¹⁷ Paragraph 3 of the same article established that no contracting party could alter its commitment to the schedule of concession (alter its method of determining dutiable value or of converting currencies so as to impair the value of any of the concessions);²¹⁸ otherwise, it should bring the matter directly to the attention of the other contracting party. If there was no agreement between the parties, they

²¹⁴ GATT determines how the schedule of concessions can be modified:

With respect to the parts subject to the rectification procedure, each contracting party needs to draw up a draft certification containing those rectified parts according to the existing procedure of GATT The draft certification will automatically be put into effect, if no objection should be raised from any other contracting party within three months after the circulation of the draft. With respect to the negotiated parts, each contracting party needs to draw up such documents after the completion of Article XXVIII negotiations, as described in Annexes A & B of C/113 and Corr.1, which contain the results of those negotiations among contracting parties concerned, and then to put them into effect through the domestic procedure. After these procedures have been completed, each contracting party incorporates the results of the negotiations into the GATT Schedules through the certification procedure (5th and 8th paragraphs of C/113 and Corr.1 and the first paragraph of L/4962). GATT, Committee on Tariff Concessions, *Loose-Leaf Schedules based on the Harmonized System Nomenclature*. Paper submitted by the delegation of Japan. GATT Doc. TAR/W/51 (1985), online: WTO <http://docsonline.wto.org/gen_search/asp>.

²¹⁵ See GATT Art. XXVIII:2.

²¹⁶ See GATT Art. II (a).

²¹⁷ GATT Art. II (b):

The products described in Part I of the Schedule relating to any contracting party, which are the products of territories of other contracting parties, shall, on their importation into the territory to which the Schedule relates, and subject to the terms, conditions or qualifications set forth in that Schedule, be exempt from ordinary customs in excess of those set forth and provided therein. Such products shall also be exempt from all other duties or charges of any kind imposed on or in connection with the importation in excess of those imposed on the date of this Agreement or those directly and mandatorily required to be imposed thereafter by legislation in force in the importing territory on that date.

²¹⁸ GATT Art. II:3 establishes that “[n]o contracting party shall alter its method of determining dutiable value or of converting currencies so as to impair the value of any of the concessions provided for in the appropriate Schedule annexed to this Agreement”.

should further negotiate along with other contracting parties interested in the matter to reach a compensatory adjustment of the matter.²¹⁹

On agriculture, a contracting party could use *GATT 1947* Art. II to challenge agricultural subsidies that exceeded the limits established in the *GATT 1947* schedules and nullified benefits given to the contracting party. According to *GATT 1947* Art. II:5, the parties involved should try to reach an agreement if one of them believed that its benefits contemplated by a concession in the appropriate schedule annexed to the *GATT 1947* had been impaired or nullified. If the parties did not reach an agreement, they could allege that they had a benefit nullified or impaired and challenge the measure of the other contracting party under *GATT 1947* Art. XXIII 1(b), stating that the modification of the commitment on the schedule of concession of the other contracting party conflicted with the provision of *GATT 1947* Art. II.

TRSC Art. 8 established that signatories agreed not to use export subsidies in a manner inconsistent with the Agreement itself. The TRSC established three effects that should be avoided in the use of subsidies: injury, serious prejudice and nullification or impairment of the benefits accruing another signatory under the *GATT 1947*. Footnote 24 established that “benefits accruing directly or indirectly under the General Agreement included the benefits of tariff concessions bound under Article II of the General Agreement.”²²⁰ These three effects, later described in the TRSC, were established under the *SCM Agreement* as requirements to

²¹⁹ *GATT* Art. II:5:

If any contracting party considers that a product is not receiving from another contracting party the treatment which the first contracting party believes to have been contemplated by a concession provided for in the appropriate Schedule annexed to this Agreement, it shall bring the matter directly to the attention of the other contracting party. If the latter agrees that the treatment contemplated was that claimed by the first contracting party, but declares that such treatment cannot be accorded because a court or other proper authority has ruled to the effect that the product involved cannot be classified under the tariff laws of such contracting party so as to permit the treatment contemplated in this Agreement, the two contracting parties, together with any other contracting parties substantially interested, shall enter promptly into further negotiations with a view to a compensatory adjustment of the matter.

²²⁰ See TRSC n. 24.

characterize adverse effects.²²¹ *SCM Agreement* Footnote 12 established that the term “nullification or impairment” was used in the *SCM Agreement* in the same sense as it was used in the *GATT 1947*.²²²

Therefore, the notion of nullification or impairment (*GATT 1947* Art. XXIII 1(b)) was related with *GATT 1947* Art. II, which established the schedules of concessions because they were part of the benefits accruing directly or indirectly to *GATT 1947* contracting parties that could be nullified or impaired. Nothing impeded *GATT 1947* contracting parties directly challenging agricultural subsidies that had exceeded the limits established in *GATT 1947* schedules under Art. II without using *GATT 1947* Art. XXIII 1(b). *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products (Canada – Dairy)*²²³ was one of the *GATT 1947* Art. II cases, among others. However, if an agricultural subsidy was given in excess of what was established in the schedule of concession of a contracting party, it might, according to *GATT 1947* Art. XXIII 1(b), nullify or impair a benefit to the other contracting party. The *EEC – Oilseed I* case exemplified this.

I.4.2.1.1 *EEC – Oilseeds I* Case and the Threshold for Challengeability under *GATT 1947* Art. XXIII and XVI

European Economic Community – Payments and Subsidies Paid to Processors and Producers of Oilseeds and Related Animal- Feed Proteins [EEC – Oilseeds I] proved that agricultural subsidies that impaired a benefit given through schedules of concessions could be successfully challenged under *GATT 1947* Arts. II and XXIII with a less complex threshold if

²²¹ See *SCM Agreement* Art. 5.

²²² See *SCM Agreement* n. 12.

²²³ Panel Report, *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products*. (1999) WTO Doc. WT/DS103/R, WT/DS113/R at paras. 125 to 130 adopted 27 October 1999, as modified by Appellate Body Report WT/DS103/AB/R, WT/DS113/AB/R, DSR 1999:VI, 2097 [*Canada – Dairy*].

compared with the market-effect requirements of *GATT 1947* Art. XVI. The EEC tried to state that a violation of an agricultural subsidy's regulation should be evaluated under Art. XVI, but the panel did not rule in this way.

On April 22, 1988, the US requested that the CONTRACTING PARTIES establish a panel on the EEC's payments and subsidies paid to processors and producers of oilseeds and related animal-feed proteins under the allegation of violation of *GATT 1947* Article XXIII and Article II. The US alleged that the EEC oilseed and related animal-feed proteins regime paid large amounts of subsidies to the EEC producers of oilseeds and related animal-feed proteins, which caused severe market distortions and significant damage to United States exports to the EEC. It argued that these subsidies, along with the processor preference payments, constituted a *prima facie* case of nullification and impairment of tariff concessions granted by the EEC in 1962 under *GATT 1947* Article II.

The terms of reference were established on June 1, 1989, as the following: "[t]o examine, in the light of the relevant *GATT 1947* provisions, the matter referred to the CONTRACTING PARTIES by the US in document L/6328 and to make such findings as will assist the CONTRACTING PARTIES."²²⁴

The US considered that the benefits accruing to it under the tariff concessions on oilseeds and oilcakes had been nullified under Article XXIII:1(b) because of a later introduction of subsidies on EEC oilseeds and protein animal feed components. The EEC considered that there were no *GATT 1947* – specific provisions for a presumption of nullification and impairment in

²²⁴ *EEC - Oilseeds I supra* note 54 at 1. *European Economic Community – Follow-Up on the Panel Report "Payments and Subsidies Paid to Processors and Producers of Oilseeds and Related Animal-Feed Proteins [EEC – Oilseeds II]* followed up the decision of the *EEC – Oilseeds I* according to the request of the US to determine whether measures taken by the EEC eliminated the impairment. The panel recommended that "the Community should act expeditiously to eliminate the impairment of tariff concessions." *GATT Panel Report, European Economic Community – Follow-Up on the Panel Report "Payments and Subsidies Paid to Processors and Producers of Oilseeds and Related Animal-Feed Proteins"*, DS28/R, 31 March 1992. BISD 39S/91

relation to the impact of production subsidies on concessions bound under Article II. It alleged that agricultural subsidies with an impact on exports were regulated by *GATT 1947* Article XVI, which required displacement²²⁵ of exports to prove adverse effects caused by subsidies. The EEC alleged that, for this reason, nullification or impairment in terms of Article XXIII:1(b) had not been established.

The EEC corroborated the requirement that the adverse effects of subsidization on imports of bound products must be established under Article XVI and TRSC Articles 8.3 and 8.4. In the view of the EEC, displacement had to be proved in order to make a challenge to their agricultural subsidies possible. They alleged that TRSC Article 8.4 provided that "the adverse effects to the interests of another signatory required to demonstrate nullification or impairment or serious prejudice may arise through ... the effects of the subsidy in displacing or impeding the imports of like products into the market of the subsidizing country."²²⁶

It stated that displacement should guide the interpretation and application of *GATT 1947* Art. XVI in the case of alleged nullification through subsidies on concessions granted under Article II. Furthermore, these provisions confirmed the principle enunciated in the TRSC that the adverse effects of subsidies in such a case could not be presumed but had to be demonstrated by the complainant.

The US stated that tariff concessions on oilseeds and oilcakes were the main concerns in the *GATT* process of liberalizing world trade. The general purpose of the *GATT 1947* was to facilitate this type of concession and to ensure that tariff obligations established in accordance with Article II were not harmed by other measures. They alleged that domestic subsidies could diminish the value of tariff concessions by artificially expanding production and making

²²⁵ In 1988 the TRSC rules, which included displacement as a requirement for challengeability under *GATT* Art. XVI, were valid for the contracting parties that had accepted and signed the Code, among them the US and the EC.

²²⁶ *EEC–Oilseeds I supra* note 54 at 13 para. 51.

domestic products artificially competitive with imports. According to them, such measures had long been recognized as being capable of nullifying or impairing benefits accruing to a contracting party within the meaning of Article XXIII:1(b).

The US quoted other GATT panel reports as examples that nullification or impairment of a benefit accruing to one contracting party occurred if domestic subsidies were given or withdrawn by another contracting party after the adoption of the tariff concession. In *The Australian Subsidy on Ammonium Sulphate* case [*Australia – Ammonium Sulphate*]²²⁷ the panel found that Australia's decision in 1949 to discontinue subsidizing the sale of one fertilizer on which Australia had granted Chile a duty-free binding in 1947 while continuing to subsidize another fertilizer nullified and impaired benefits accruing to Chile as a result of the tariff concessions granted by Australia on sodium nitrate. The 1985 Panel Report on *European Economic Community – Production Aids Granted on Canned Peaches, Canned Pears, Canned Fruit Cocktail and Dried Grapes* [*EEC – Canned Fruit*]²²⁸ was also referred to by the US in support of the principle outlined above.

The US noted that subsidies granted after a tariff concession constituted nullification and impairment according to the 1955 ruling of the CONTRACTING PARTIES at the 1954-55 ReviewSession, which provided that:

So far as domestic subsidies are concerned, it was agreed that a contracting party which has negotiated a concession under Article II may be assumed, for the purposes of Article XXIII, to have a reasonable expectation, failing evidence to the contrary, that the value of a concession will not be nullified or impaired by the

²²⁷ *The Australian Subsidy on Ammonium Sulphate* (1950), GATT Doc. CP.4/39, 2nd Supp. B.I.S.D 188 [*Australia – Ammonium Sulphate*].

²²⁸ *European Economic Community – Production Aids Granted on Canned Peaches, Canned Pears, Canned Fruit Cocktail and Dried Grapes* (1985), GATT Doc. L/5778, unadopted [*EEC – Canned Fruit*].

contracting party which granted the concession by the subsequent introduction or increase of a domestic subsidy on the product concerned.²²⁹

In order to prove a violation of *GATT 1947* Art. XXIII, the US had to prove that it had a reasonable expectation that the EEC subsidies would not be applied and nullified its benefits previously given according to the levels determined in the tariff schedules. The EEC reasoned that *GATT 1947* Arts. III:8(b) and XVI:1 explicitly authorized agricultural production subsidization, and this right would be violated if the panel ruled that there was an impairment of tariff concessions.²³⁰

Moreover, the EEC stressed again that violation of non-tariff measures could only be verified by specific *GATT 1947* provisions that regulated each one. Subsidies were one of these measures that had their own special rules established in Article XVI.

The panel held that benefits accruing to the US under Article II of the *GATT 1947* in respect of the tariff bindings for oilseeds in the EEC Schedule of Concessions had been impaired. The impairment was a result of the introduction of agricultural subsidies that protected EEC producers of oilseeds from the movement in prices of imports and thereby prevented the tariff concessions from having any impact on the competitive relationship between domestic and imported oilseed. The panel recommended that the EEC consider ways and means to eliminate the impairment of its tariff concessions for oilseeds.

This case demonstrated that agricultural subsidies could be challenged under *GATT 1947* Arts. II and XXIII without any need to prove any market-effect distortion, such as displacement. But the subsidies had to nullify or impair a concession previously given to another country in order to be successfully challenged. *GATT 1947* Art. XXIII also could be used to challenge

²²⁹ *Review Reports GATT, Report by the Working Party on "Other Barriers to Trade" adopted on 3 March 1955*, 3rd Supp. B.I.S.D. 222 at para. 13.

²³⁰ *EEC–Oilseeds I supra* note 54 at 35.

agricultural subsidies that were given in manner inconsistent with *GATT 1947* Art. III:8(b), as will be verified in the next section.

I.4.3 *GATT 1947* Article III—National Treatment and Related Provisions

GATT 1947 Art. III:8(b) authorized the use of subsidies “exclusively to domestic producers,” which included payments derived from internal taxes or other charges and subsidies “through governmental purchase of domestic products.”²³¹ This provision opened up possibilities for agricultural subsidizing, but they could be directly challenged through *GATT 1947* Art. XXIII 1(b) if the given domestic subsidy nullified or impaired any benefit previously given to a Member. Challengeability of agricultural subsidies under Art. III and Art. XXIII 1(b) also had a less complex threshold than Art. XVI, because there were no market-effect requirements for challengeability.

GATT 1947 Article III regulated national treatment. Basically, it states that imported products could not receive treatment less favorable than that for domestic like products, with some exceptions. The rationale was to limit the use of protectionist trade practices and prevent discrimination against imported goods. The clause prohibited contracting parties from imposing internal taxes, or other internal charges of any sort, in surplus of those applied, directly or indirectly, to like domestic products.²³²

GATT 1947 Art. III:4 specifically determined that products imported from other GATT Members could not be treated less favorably in comparison with like products of national origin

²³¹ See *GATT 1947* Art. III:8 (b)

²³² See *GATT 1947* Art. III:2

in respect of “all laws, regulations and requirements affecting their internal sale, offering for sale, purchase, transportation, distribution or use.”²³³

However, paragraph 8 of the same Art. III of the *GATT 1947* set up some exceptions and allowed different treatment for national products under special circumstances. Paragraph (a) waived products purchased for governmental purposes, excluding goods bought for commercial reasons. Paragraph (b) established that the provisions of Art. III shall not prevent the payments of subsidies (agricultural or not) to domestic producers, including payments derived from internal taxes and subsidies of governmental purchases of domestic goods. Paragraph (b) was an important exception during the GATT years, because it excluded subsidies in general from the principle of “nondiscrimination” of *GATT 1947* Art. III, thereby making legal²³⁴ the payment, exclusively for domestic producers, of direct governmental subventions involving “the expenditure of revenue by a government.

On agriculture, a country could apply *GATT 1947* Art. III to challenge agricultural subsidies given exclusively to domestic products that involved an expenditure of revenue by a government. Also, paragraph 9 established that the provisions of Article III could have prejudicial effects on the interests of exporting countries; therefore, any measure taken under Art. III should be taken “with a view to avoiding to the fullest practicable extent such prejudicial effects.”²³⁵ At any rate, if the harmed exporting country had a benefit nullified or impaired, it could challenge the measure of the other contracting party under *GATT 1947* Art. XXIII 1(b).

²³³ See *GATT 1947*, Art. III, para. 4.

²³⁴ In *Indonesia – Autos* the panel rejected the Indonesian allegation based on the exception of GATT Art. III 8(b) and concluded that only subsidy payments made directly to producers were covered by this exception and held that tax exemptions did not constitute such payments. Panel Report, *Indonesia – Certain Measures Affecting the Automobile Industry* (1998), WTO Doc. WT/DS/54/R, WT/DS55/R, WTDS59/R and WT/DS64/R and Corr.1 and 2, at paras. 14.118-122 adopted 23 July 1998, and Corr. 3 and 4, DSR 1998:VI, 2201 [*Indonesia – Autos*].

²³⁵ See *GATT 1947* Art. III para. 9.

The allegation would be that the modification of the commitment of the schedule of concession of the other contracting party conflicted with the provision of *GATT 1947* art. III.

In *Canada – Certain Measures Concerning Periodicals* [*Canada – Periodicals*],²³⁶ a Canadian Crown Corporation applied reduced postal rates to Canadian periodicals. According to Canada, the reduced postal rate could be considered as “payment of subsidies exclusively to domestic producers.” Consequently, Canada stated that *GATT 1947* Article III: 8 (b) exempted the reduced postal rate from the regulation in Article III: 4. The Appellate Body did not agree with the Canadian allegation and found that Article III: 8 (b) could not be applied in this case because the transfer was from one governmental entity to another.

In *Indonesia – Autos*, the panel decided that tax exemptions could not be given only to national producers under the exception of *GATT 1947* Art. III: 8 (b). It ruled that “the purpose of Article III:8(b) is to confirm that subsidies to producers do not violate Article III, as long as they do not have any component that introduces discrimination between imported and domestic products. In the view of the panel, the wording ‘payment of subsidies exclusively to domestic producers’ exists so as to ensure that only subsidies provided to producers, and not tax or other forms of discrimination on products, be considered subsidies for the purpose of Article III:8(b) of *GATT 1947*.”²³⁷

The cases above clearly limited the exemption of subsidization from Article III: 8 (b). Even though they were non-agricultural subsidy cases, they confirmed that the GATT legal decisions were being made in such a way as to limit the use of subsidies under the exception of

²³⁶ In the Report of the Appellate Body it was determined that *GATT 1947* Art. III 8(b) exempted only payment of subsidies “that involved the expenditure of revenue by a government”. The decision was supported by *GATT 1947* Art. III:2 and III:4 and by a similar decision in GATT Panel Report, *United States – Measures Affecting Alcoholic and Malt Beverages* (1992) WTO Doc. WT/DS23/R adopted 19 June 1992, BISD 39S/206 [US – *Malt Beverages*]. Appellate Body Report, *Canada – Certain Measures Concerning Periodicals* (1997), WTO Doc. WT/DS31/AB/R at 32-34 adopted 30 July 1997, DSR 1997:I, 449 [*Canada – Periodicals*].

²³⁷ *Indonesia – Autos* *supra* note 234 at para. 14.113.

GATT 1947 Art. III: 8 (b), which was a steady step towards trade liberalization. The GATT's contracting parties tried to use the exception of Art. III: 8 (b) to give discriminatory indirect subsidies, but this practice was condemned by legal decisions. GATT panels could find ways to use *GATT 1947* existing provisions to keep condemning subsidization practices in a consistent way, as is going to be verified in the following case.

I.4.3.1 The *EEC – Canned Fruit Case* and the Concept of “Trade Damage”

In October 1981, US peach producers filed a non-violation complaint²³⁸ about EEC subsidies on raw materials given to fruit processors. The US alleged that these subsidies had violated *GATT 1947* Articles XXIII:1(b), and the EEC argued that they could not be challenged because they complied with the exception to Art. III:8(b).

This time, the EEC producers of canned peaches, canned pears, fruit cocktail and dried grapes were receiving subsidies to equalize the cost of raw materials. In this case, the subsidy was based on the selling price of imported canned fruit, and for this reason, the EEC was equalizing all differences in costs between EEC and imported foreign products inside the national market.

The consultations started in December 1981. The US claimed that EEC subsidies for canned fruit had nullified the benefits of tariff concessions on the processed fruit products involved. It was a claim with the following terms of reference:

To examine, in the light of the relevant GATT provisions, the matter referred to the CONTRACTING PARTIES by the United States relating to production aids granted by the European Economic Community on the production of canned peaches, canned pears, fruit cocktail and dried grapes (L/5306), and to make such

²³⁸ See *supra* note 211.

finding as will assist the CONTRACTING PARTIES in making recommendations or rulings as provided for in Article XXIII.²³⁹

The case was legally based on *GATT 1947* Article XXIII:1(b),²⁴⁰ but the EEC alleged that, even though it was a non-violation case, the domestic subsidy could not be determined as illegal under *GATT 1947* rules, because it was allowed by the exception of *GATT 1947* Article III:8(b).²⁴¹ On the other hand, the US alleged that EEC subsidies were harming earlier US tariff concessions, which characterized a nullification or impairment of concession regulated by *GATT 1947* Article XXIII:1(b).

The EEC responded that most of its tariffs for processed fruit were bound and could not be changed. That being the case, if all compensatory subsidies were considered nullification or impairment of any GATT benefit, it would be impossible to compete with imported products. The EEC also alleged that specific compensatory measures could never be considered as impairment or nullification of benefits, because they simply corrected cost distortions, and the US was not able to prove any trade damage resulting from the given subsidies. The US countered that the EEC was over-compensating.

The panel ruled that the processor subsidy on dried grapes did not constitute neither violation nor nullification and impairment, because the US “could have reasonably anticipated during the various tariff negotiations Greek producers and processors would continue to benefit

²³⁹ *EEC – Canned Fruits supra* note 228.

²⁴⁰ *GATT 1947* Article. XXIII 1(b):

If any contracting party should consider that any benefit accruing to it directly or indirectly under this Agreement is being nullified or impaired or that the attainment of any objective of the Agreement is being impeded as the result of: ... (b) the application by another contracting party of any measure, whether or not it conflicts with the provisions of this Agreement, or ...

²⁴¹ *GATT 1947* Article. III 8(b) states:

The provisions of this Article shall not prevent the payment of subsidies exclusively to domestic producers, including payments to domestic producers derived from the proceeds of internal taxes or charges applied consistently with the provisions of this Article and subsidies effected through governmental purchases of domestic products.

from support prices.”²⁴² However, it stated that subsidies on the canned fruit did constitute nullification and impairment:

The Panel concluded that the production aids granted by the EEC since 1978 to processors of peaches and since 1979 to processors of pears nullified or impaired benefits accruing to the United States from tariff concessions granted by the EEC under Article II of the General Agreement in 1974 on canned peaches, canned pears and canned fruit mixtures and in 1979 on canned pears.²⁴³

The panel determined that no other artificial disadvantage could be imposed on the US in receiving the tariff concession on canned fruits. The panel also recommended that the EEC consider ways and means to restore the competitive relationship between imported US and domestic EEC canned peaches, canned pears and canned fruit cocktail and invited the EEC to report within a reasonable, specified period on action taken in line with the panel’s recommendation.²⁴⁴

The most important US victory in the case was that the panel ruled that even a finding of non-violation, nullification and impairment did not require proof of damage and, for this reason, determined the impairment even with no proof of “trade damage”:

The Panel was of the view that it was not necessary to establish statistical evidence of damage in order to make a finding of nullification and impairment under Article XXIII. It noted that this view had also been adopted in the Panel report on Treatment by Germany of Imports of Sardines (BISD 1S/56, para. 9). Benefits accruing from bound tariff concessions under Article II also encompass future trading opportunities. Consequently, complaints by contracting parties regarding nullification and impairment should be admissible even if there was not yet statistical evidence of trade damage. The Panel was convinced that, in this case, it possessed sufficient evidence to make a finding of nullification and impairment without recourse to the statistical evidence submitted by both parties. The Panel decided therefore to include neither the statistical data regarding trade

²⁴² *EEC – Canned Fruits supra* note 228 at 22 n. 32.

²⁴³ *Ibid.* at 21.

²⁴⁴ *Ibid.* at 23.

damage nor its written analysis of this data in its report to the CONTRACTING PARTIES.²⁴⁵

If the panel had decided that proof of “trade damage” was required to prove nullification of a benefit under Art. XXIII 1(b), the threshold for challengeability would have considerably risen, because it would have required a market-effect analysis. The panel, however, used the same rationale as that of previous GATT decisions, to condemn agricultural subsidies with no need of a market-effect proof.

The analysis of the cases demonstrated that challengeability under *GATT 1947* Art. XXIII 1(b) had a lower threshold than Art. VI and Art. XIV because of the lack of market-effect requirements. Art. XXIII 1(b) could be the legal basis for challenges under *GATT 1947* Art. II (if subsidies nullified or impaired a concession previously given) and *GATT 1947* Art. III (if subsidies were given in a manner inconsistent with Art. III:8(b)) or even when there was no violation of any *GATT 1947* provision (non-violation cases based on *GATT 1947* Art. XXIII 1(b)).

The substantive analysis of the three articles through which it was possible to challenge agricultural subsidies during the GATT years and the related cases demonstrated that there was a rationale to condemn agricultural subsidies and trade-restrictive practices during the GATT years. The fact that some decisions were not complied with involves a dimension that goes beyond a legal analysis, because it has political roots and is related with the balance of power during the GATT years, which will be analyzed next.

²⁴⁵ *Ibid.* at 21.

I.5 The GATT Agenda for Agriculture Before the Uruguay Round – The US Waiver and the Balance of Power

During the first 20 years of the GATT, the US set its agenda as a result of its role as leader. This was the reason that, despite the strong opposition of the EC,²⁴⁶ agriculture was included in the issues regulated by the GATT. However, the US had a bipolar policy regarding agricultural subsidies during the first years of the GATT. At the same time that the country required trade liberalization, it did not want to eliminate its domestic barriers for agricultural imports, as its request for a waiver demonstrated.

I.5.1 The US Waiver

In the same year that rules against subsidies were being strengthened, 1955,²⁴⁷ the US asked to be waived from the general elimination of quantitative restrictions of Art. XI of the *GATT 1947*:

The United States requests that there be placed on the Agenda of the Ninth Section for consideration by the CONTRACTING PARTIES a request by the United States for a waiver of obligations under the Agreement with respect to the use of Section 22 of the Agricultural Adjustment Act as amended.²⁴⁸

²⁴⁶ The EC since the GATT years has opposed liberalization on agriculture because of its Common Agriculture Policy [CAP].

²⁴⁷ *Supra* note 15.

²⁴⁸ GATT, Report of the Working Party. *Waiver Granted to the United States in Connexion with Section 22 of the United States Agricultural Adjustment Act*, GATT L/464 of 30 November 1955, 10th Sess., L/464, online: WTO <http://www.wto.org/gatt_docs/English/SULPDF/90690238.pdf> at 1 [GATT US Waiver].

GATT 1947 Article XI regulated the elimination of quantitative restrictions through a general prohibition of quotas, import or export licenses and other measures. One of the exceptions²⁴⁹ to the general prohibition included restrictions for agricultural products.

Article XI (2) established the exceptions for the general prohibition on quantitative measures: (a) measures that allowed export prohibitions or restrictions of a temporary nature to avoid food shortages in the exporting country; (b) measures that also allowed for import and export restrictions (not prohibitions) necessary to the application of standards or regulations of the classification, grading or marketing of commodities in international trade; and the most significant exception for this study, (c) measures that allowed import restrictions on any agricultural or fisheries product where necessary: (i) to enforce domestic restrictions on the marketing or production of a similar product, (ii) to eliminate a temporary surplus of a like product or (iii) to restrict the quantities of any animal product, if the amount of the compatible national product was relatively negligible.²⁵⁰

Article XI:2 (c) permitted quantitative restrictions on the importation of agricultural products necessary for a national policy restricting domestic production, under the condition that the proportions between imported and domestic products remained “what it would reasonably be expected in the absence of any restriction.”²⁵¹ If the *GATT 1947* could not completely avoid restrictive measures, it found a way to keep market stability as much as possible after the

²⁴⁹ *GATT 1947* Article XI states that:

No prohibition or restrictions other than duties, taxes or other charges ... shall be instituted or maintained ... on the importation of any product or on the exportation of any product... 2. The provisions of this paragraph did not apply to ... (a) ... prevent or relieve food shortage, (b) ... necessary to application of standards for the classification, or marketing of commodities and (c) import restrictions in any agricultural or fisheries product imported to enforce governmental measures...

²⁵⁰ *Ibid.*

²⁵¹ *GATT 1947* Art. XI: 2 last paragraph:

[...] Moreover, any restrictions applied under (i) above shall not be such as will reduce the total of imports relative to the total of domestic production, as compared with the proportion which might reasonably be expected to rule between the two in the absence of restrictions. In determining this proportion, the contracting party shall pay due regard to the proportion prevailing during a previous representative period and to any special factors which may have affected or may be affecting the trade in the product concerned.

imposition of restrictive measures. According to this rule, if a contracting party had a consumption market of 10 tons of soybeans (50% produced in the national market and 50% imported from another contracting party), the other contracting party would be entitled to a share of five tons. The problem with this rationale was that determining market share involved other market-effect variables that were difficult to establish. One of these variables was, for example, price distortion caused by domestic subsidies in the import-restricting country.

Furthermore, if the restriction kept the same trade balance between domestic/imported products, quantitative restrictions would not be an attractive tool for agricultural protection. In this case, the import-restricting country would have the same or almost the same market share that would exist in the absence of protection. This threshold for challengeability to impose quantitative restrictions for agricultural imports was difficult to be complied with; that is the reason the US asked for the waiver. In this way, the country did not have to comply with such a high threshold to impose quantitative restrictions for imports of agricultural products. The US also swerved from compliance with *GATT 1947* Art. VI, which required a determination of material injury to domestic industry from subsidized imports before countervailing duties could be imposed.

The US alleged that it had maintained a system of agricultural subsidies and that the prices of some of its agricultural products were higher than the levels prevailing in other parts of the world. For this reason, the American Congress had enacted Section 22 of the Agricultural Adjustment Act, which provided that, whenever the President of the United States found that products were being imported in quantities that “render[ed] ineffective” or “materially

interfere[ed]” with its agricultural support programs, he could impose quotas or any other quantitatively restrictive measure to prevent imports.²⁵²

The GATT Protocol of Provisional Application obligated the contracting parties to comply with Part II of the Agreement (Articles III to XXIII, inclusive) only “to the fullest extent not inconsistent with existing legislation.”²⁵³ Therefore, if a country alleged that any provision of Part II was inconsistent with its existing legislation, it could choose to not comply with Part II. As such, the American position of non-compliance was consistent with the GATT rules.

The waiver was granted to the US, exempting the country from the general elimination of quantitative restrictions of Art. XI of *GATT 1947*:

The CONTRACTING PARTIES DECIDE, pursuant to paragraph 5(a) of Article XXV of the General Agreement and in consideration of the assurances recorded above, that subject to the conditions and procedures set out hereunder the obligations of the United States under the provisions of Articles II and XI of the General Agreement are waived to the extent necessary to prevent a conflict with such provisions of the General Agreement in the case of action required to be taken by the Government of the United States under Section 22, The text of Section 22 is annexed to this Decision;²⁵⁴

Accordingly, the US was disobliged from compliance with the requirements (trade proportion between national/imported products at the expected rate of absence of any restriction) to impose quotas on agricultural imports. It is relevant to observe that these conditions for application of restrictions on agricultural imports had problems in being enforced exactly because they were based on market-effect variables. This was one of the few market-effect rules of the GATT and not by any coincidence – it had problems in being enforced.

²⁵² *Ibid.*

²⁵³ Economic and Social Council United Nations, Second Section of the Preparatory Committee of the United Nations Conference on Trade and Employment, e/pc/t/202, “Text of Protocol of Provisional Application as amended up to September 18, 1947 by the Tariff Agreement Committee”(1947) at 1.

²⁵⁴ *GATT US Waiver supra* note 248 at 1.

Therefore, contracting parties kept applying agricultural quantitative restrictions, but GATT panels limited this application to defend trade liberalization in agriculture, as is going to be seen in the following case: disregarding the legal requirement of *GATT 1947* Article XI (c).²⁵⁵

I.5.1.1 The *US – Dairy Case* and the US Waiver

This case proved that, in some circumstances, where *GATT 1947* regulations allowed agricultural barriers, the panels worked to restrict the application of such barriers, which helped trade liberalization over the GATT years. It also exemplifies how the US waiver influenced the GATT system and its decisions.

In this case, the US demonstrated its strength and power during the GATT years, because it clearly declared that its quotas were not consistent with *GATT 1947* rules, but the country would keep them. It also declared that it would leave the *GATT 1947* if it was obliged to comply with the decision from the Working Party.²⁵⁶ However, despite US pressure, the decision declared that American import restrictions on dairy products were not applied along with domestic restrictions on the production of the raw material for the products²⁵⁷ and, for this

²⁵⁵ In *Turkey – Restrictions on Textiles* the panel observed that, since the first years of the GATT, contracting parties had difficulties in not imposing quantitative restrictions, especially for agriculture: Notwithstanding this broad prohibition against quantitative restrictions, GATT contracting parties over many years failed to completely respect this obligation. From the early years of the GATT, in sectors such as agriculture, quantitative restrictions were maintained and even increased to the extent that the need to restrict their use became central to the Uruguay Round negotiations. Panel Report, *Turkey – Restrictions on Imports of Textile and Clothing Products* (1999), WTO Doc. WT/DS34/R at para. 9.64 adopted 19 November 1999, as modified by Appellate Body Report WT/DS34/AB/R, DSR 1999:VI, 2363[*Turkey –Textiles*].

²⁵⁶ Hudec defines working parties:

Working parties were small ad hoc negotiating bodies consisting of a cross-section of GATT's Membership—the governments directly interested the major powers, and representatives of constituencies such as the Nordic countries or the developing countries. Normal working party practice allowed the parties to the dispute to vote like everyone else, a practice that almost always assured a divided working party over contested issues. But the strong legal consensus allowed GATT to extract legal rulings from these reports anyway. [Hudec, *Enforcing Trade Law*] *supra* note 17 at 29-30.

²⁵⁷ Trebilcock, *The Regulation of Trade* *supra* note 29 at 193

reason, were not consistent with the GATT rules. This decision demonstrates the legal rationale in GATT decisions to condemn practices that went against trade liberalization. The influence of the leading power countries at that time could avoid compliance because of procedural rules, but they could not avoid consistent decisions that condemned trade-restrictive practices against all the pressure of some powerful interests.

The *United States – Import Restrictions on Dairy Products (US – Dairy)* case involved the interpretation of several articles of the *GATT 1947* that regulated agriculture, mainly the agricultural exceptions of Article XI. The dispute was about illegal dairy import quotas imposed in 1951 by the US on these products coming from Australia. The import quotas on dairy products imposed by the US were mainly on butter, milk powder and casein, among others. Despite this, cheese was the main concern of the complaints, because some countries in Europe, such as the Netherlands, were starting to export this product after World War II.²⁵⁸

During the proceedings, the US knew that the dairy quota was a violation of *GATT 1947* Article XI. The US only asked the parties to wait for the next American political events that could change the restrictive measures. In the words of the US representative, “The United States remained as firmly committed to expansion of world trade as before. Section 104 (that established the dairy quotas), it seemed, was a freakish accident.”²⁵⁹

Even with all the pressure against it, the dairy quota was renewed but with some liberalizing amendments. The most significant of them was the possibility of the President’s increasing the 1951 dairy quota amounts. Obviously, the dairy exporting countries, even with

²⁵⁸ United States. Congress. Senate. Committee on Banking and Currency, *Hearings on the Defense Production Act Amendments of 1951 Before the Senate Committee on Banking and Currency, 82d Cong., 1st Sess.* (Washington D.C.: US Govt. Print. Off., 1952) at 1895.

²⁵⁹ GATT, *Item 30 – Restrictions on Imports of Dairy Products into the United States - Addendum - Memorandum by the United States Delegation*, GATT/C.P.6/28/Add/1 of 24 Sept. 24 1951, 6TH Sess., online: WTO <http://www.wto.org/gatt_docs/English/SULPDF/90070366.pdf>

the US decision to raise the quota levels for several dairy products, did not welcome this decision.

The GATT Working Party designated to settle this case held that American import restrictions on dairy products were not accompanied by domestic restrictions on the production of the raw material for the products²⁶⁰ and, for this reason, were violating *GATT 1947* Article XI. Furthermore, the US recognized that dairy quotas were a violation of GATT obligations.

The idiosyncratic solution to the problem of the American violation suggested by the third-party decision was a reduction of 12,000 metric tons in the US exports of wheat flour instead of the 15,000 previously requested by the Netherlands. The criteria used by the third party to reach the number of 12,000 metric tons are not known. The Netherlands formally implemented the quotas in 1953. However, in 1955, the US obtained a waiver that exempted the country from compliance with *GATT 1947* Article XI, which, therefore, also exempted the country from acting in accordance with the *US – Dairy* quota's decision.

It is relevant to mention that, during the 10th section of the Working Party that authorized the US to have the waiver, the last paragraph was a rule related to the dairy case:

The Working Party recognized that a number of contracting parties had indicated that they continued to suffer serious damage from the application of import restrictions on dairy products. In view of the indication given by the Government of the Netherlands that concessions granted by the United States Government have been impaired, and as the restrictions have not been relaxed since the date of the Resolution of 5 November 1954, the Working Party agreed to recommend that the Government of the Netherlands, having recourse to the provisions of Article XXIII, be authorized to suspend the application to the United States of its obligations under the General Agreement to the extent necessary to allow it to apply a limit of 60,000 metric tons on imports of wheat flour from the United States during the calendar year 1956.²⁶¹

²⁶⁰ *United States – Import Restrictions on Dairy Products* (1953), 2d Supp. B.I.S.D. (1954) 28 [*US – Dairy*]

²⁶¹ *GATT US Waiver supra* note 248 at 3-4.

The example of this case is idiosyncratic because the panel authorized cross-retaliation, which meant that the harmful effects that the Netherlands felt in the international dairy market because of the US import restrictions for this product could be compensated in the wheat trade market. The legal analysis of the panel was consistent and clear, but the US did not comply with the decision, because the country obtained the waiver after this case was decided. The lack of compliance in this case was not a flaw in the *GATT 1947*'s legal framework itself. Several international treaties allow reservations.

Therefore, it can be stated that the hypothetical problem of lack of compliance during the GATT years—if there was such a thing—was not caused by any “flaw” in the legal system. In this case, the US did use a possible legal strategy, a waiver authorized by the *GATT 1947*, to keep imposing restrictions on imports. However, the panel condemned this US practice and followed the same legal rationale of previous panels that condemned trade-restrictive practices that were against trade liberalization.

However, it cannot be denied that the waiver weakened further efforts to strictly enforce Article XI against all contracting parties.²⁶² For this reason, the US had to file legal complaints requiring other contracting parties to comply with *GATT 1947* Article XI:2(c), as is going to be examined in the next section.²⁶³

²⁶² Trebilcock, *The Regulation of Trade supra* note 29 at 193.

²⁶³ It is important to note that, having been granted the waiver and because of the pressure of Section 301, the US continued to require from other Members compliance with the provisions that the country had been waived from. Section 301 is the principal statutory authority under which the United States may impose trade sanctions against foreign countries that maintain acts, policies and practices that violate, or deny US rights or benefits under trade Agreements, or are unjustifiable, unreasonable or discriminatory and burden or restrict US commerce. Section 301 of the 1974 Trade Act. Section 301 was challenged several times under WTO dispute settlement system because it is considered a “black list” of countries for possible retaliation that do not follow the US international policy. Its provisions allows the USTR – United States Trade Representative [USTR] to initiate an investigation of the trade practices of another country. There is also what is called the “Special 301” A report on intellectual property in many countries.

I.5.1.2 The *Canada – Eggs* Case and the Weaknesses Caused by the US Waiver

In September 1975, the US filed a *GATT 1947* complaint against Canada, stating that it had failed to comply with *GATT 1947* Article XI:2(c) on quantitative restrictions on the importation of eggs.²⁶⁴ The US alleged that the legal reason for this complaint was that Canada had set up a small quota for the importation of the product. Unfortunately for the US, it was complex to require compliance with this particular legal issue, from which its own compliance had been waived. The US's legal claim, therefore, was weakened due to the waiver.

According to the Report of the Working Party adopted on February 17, 1976, the US asked three questions about the Canadian quota for eggs: (i) did the Canadian supply management system on eggs conform to the requirements of *GATT 1947* Article XI, (ii) was the basis for determining the import quotas in accordance with the requirements of the last paragraph of Art. XI, and (iii) did the Canadian quotas under Article XI constitute a nullification and impairment of a prior binding?

The Working Party held that, in reference to the first question, the Canadian quota for eggs was in conformity with the requirements of Article XI:2(c)(i). It went on to declare that it was unable to reach any conclusion in regards to the second and third questions, suggesting that the US and Canada try to come to a pragmatic agreement in bilateral discussions.

Canada – Import Quotas on Eggs [*Canada – Eggs*] was not a typical *GATT 1947* case, because the US did not file a petition, but rather asked the opinion of the *GATT 1947*'s experts about the legality of the Canadian program under *GATT 1947* Article XI. This case illustrates the

²⁶⁴ Working Party Report, *Canada – Import Quotas on Eggs* (1975), GATT Doc. L/4279, adopted 17 February 1976, BISD 23S/91 [*Canada – Eggs*].

impact the US waiver had on the *GATT 1947* system. However, it cannot be stated that the waiver affected the way the *GATT 1947*'s Working Party legally analyzed the cases. It was only one more component in the scenario of divergence of interests in the GATT system, as is going to be seen in the next section.

I.5.2 The Balance of Power During the *GATT 1947* years

Even though the US led a tariff reductions movement in the Tokyo Round, and it had always strongly criticized the EEC agricultural policies of farm subsidies, at the end of 1960s, the country lined up with the EEC to support a less “rule oriented”²⁶⁵ GATT. It wanted a more diplomatic institution, because at that time, it had also implemented policies of heavy agricultural subsidization to compensate for the European agricultural support policies.

Other GATT contracting parties started to exert pressure, asking for greater “legalism,” that is, a more effective enforcement of obligations.²⁶⁶ At the heart of the issue were EEC agricultural protectionist measures and US protectionist measures that were beginning to be applied. In retaliation, the EEC started to put forward the concept of a more diplomatic rather

²⁶⁵ Celso Lafer explains: “it is precisely to refrain political unilateralism and commercial retaliation that the WTO dispute settlement system was conceived, while a *rule oriented* mechanism, according to Grocio, intended to ‘domesticate’ the unilateral tendencies of the “raison d’Etre” of the State *power oriented*”. Celso Lafer. *O sistema de solução de controvérsias da Organização Mundial do Comércio* (Porto Alegre: Livraria do Advogado, 1998) at 15[translated by the author] cited in Aluisio de Lima Campos, Fabio Carneiro Cunha “et all”, *Ensaio em Comercio Internacional: Antidumping, Disputas Comerciais e Negociacoes* (Sao Paulo: Singular, 2005). Petersmann describes rule-oriented approaches as “suggest(ing) negotiations among governments or individuals on the elaboration and observance of general rules of conduct which all participants voluntarily accept, because the rules reconcile their conflicting short-term interests with their common long-term interests in a mutually beneficial manner. On the other way around Petersman describes power-oriented approaches as discussions, negotiations or dispute settlement in which one party asserts or uses the relative power at its disposal in order to influence the conduct of the other party. Ernst-Ulrich Petersmann, *The GATT/WTO Dispute Settlement System: International Law, International Organizations and Dispute Settlement* (London: Kluwer Law International, 1997) at 44-57.

²⁶⁶ Hudec, *World Diplomacy supra* note 35 at 226.

than rule-oriented GATT. The US,²⁶⁷ facing new trade situations that aligned its trade needs with EEC priorities, started to defend the position of the EEC.

In 1982, the WTO/GATT Thirty-Eighth Session at Ministerial Level took place in Geneva with the goal of renewing the need for liberalization. According to the Draft Ministerial Declaration of July 30, 1986, contracting parties agreed that there was an urgent need to bring more discipline and predictability to the world's agricultural trade in order to correct, prevent and combat distortions and to bring about an equitable balance of rights and obligations among contracting parties. It was agreed that negotiations should focus on achieving greater liberalization of trade in agricultural products by:

- (i) improving market access through, inter alia, the reduction of import barriers;
- (ii) improving competitive conditions by increasing discipline on the use of *all subsidies affecting agricultural trade*, including the phasing-out in an agreed timeframe of export subsidies;
- (iii) recognizing the right to implement national policies, CP's will agree upon an action to redirect them and all their instruments, so as to correct market imbalances and reduce substantially their negative effects on international trade;
- (iv) handling the problem of sanitary and phytosanitary measures.²⁶⁸

It seems that the target of this initiative was the EEC's agricultural trade policy. Negotiations proceeded, but in the end, the Community did not sign the declaration. By 1985, tensions over agricultural trade were growing. The situation was aggravated during the period 1980–1985, when the EEC's subsidized exports increased, which gave the EEC a bigger share of the international agricultural market.

²⁶⁷ One of the reasons for this shift in the US position can be credited to the internal disputes of the Executive and Legislative branches. Even though Congress used to complain about the Executive's excess of power and despite several clear problems involving trade in agricultural products and textiles, Congress had generally given the Executive branch some liberty to pursue the original GATT agenda of trade liberalization. However, after those events, the US Congress wanted to participate more in international trade decisions.

²⁶⁸ GATT, *Draft Ministerial Declaration Preparatory Committee. Prep. Com.*, GATT Doc. (86) W/49 (1986), online: WTO <<http://docsonline.wto.org/gen. search/asp>> at 5-6 [emphasis added].

In 1985, the US reacted and created programs of “counter-subsidies” to compensate the US agricultural support program, such as the Export Enhancement Program [EEP].²⁶⁹ The US’s counterattack on subsidies triggered a subsidy war during the next few years, in which low and artificial world prices were driven even lower. The most affected parties were countries that also exported agriculture products but could not compete with the US and the EEC, with their high levels of subsidy.

The war resulted in the American 1985 Food Security Act, commonly known as the Farm Bill, enacted to replace the no longer effective agricultural programs in the 1981 Act. There was an expectation of change, but rather than marking a major shift in the US policy or significant reform of the subsidy programs, the bill kept the old structure of subsidies intact. No major subsidy program was reduced.

Agricultural subsidies on milk and other products continued, and efforts to regain lost export markets were made, which included new forms of subsidies.²⁷⁰ In response to these deviations and growing tensions, other leading GATT governments, including the EEC, agreed that agriculture would have to be included as a major issue in the forthcoming Uruguay Round negotiations:

[The] 1982 Ministerial Declaration established that it was needed “to bring agriculture more fully into the multilateral trading system by improving the effectiveness of *GATT 1947* rules, provisions and disciplines and through their common interpretation; to seek to improve terms of access to markets; and *to*

²⁶⁹ The Export Enhancement Program was designed to help US farm products meet competition from subsidizing countries, especially the European Union Under the program, the US Department of Agriculture pays cash to exporters as bonuses, allowing them to sell US agricultural products in targeted countries at prices below the export’s cost of acquiring them. The EEP was announced by USDA on May15, 1985. USDA, *Food Security Act of 1985* 7 U.S.C. 1736 p. et seq. online: USDA <<http://ffas.usda.gov/info/factsheets/eep.asp>>.

²⁷⁰ J. B. Penn *Public Policy Education and the 1985 Farm Bill*. (London: Economic Perspectives Inc., 1989) at 140.

bring export competition under greater discipline. To this end a major two-year work programme shall be undertaken.”²⁷¹

The influence of certain groups of countries, such as the EEC, that wanted to keep subsidizing agriculture can be noted in the Ministerial Declaration. The chapter on agriculture, and specifically the letter regulating agricultural subsidies for export, did not mention the phasing-out of agricultural exports.

The text of the Ministerial Declaration of 1982 on agricultural subsidies follows:

The operation of the General Agreement as regards subsidies affecting agriculture, especially export subsidies, with a view to examining its effectiveness, in the light of actual experience, in promoting the objectives of the General Agreement and avoiding subsidization seriously prejudicial to the trade or interests of contracting parties. Other forms of export assistance will be included in this examination.²⁷²

Only in the Ministerial Declaration of the Uruguay Round in 1986 was there a mention of phasing out agricultural subsidies. The tensions that were a result of the divergence of interests of the leading nations in the GATT were reflected in some weaknesses of the WTO system created in 1995, which will be analyzed in Part II of the dissertation.

I.6 Conclusion

The *GATT 1947* framework and panels were successful in building a legal system with a *rationale* to limit agricultural subsidization.²⁷³ Most of the decisions stated that agricultural

²⁷¹ GATT, *Ministerial Declaration Adopted on 29 November*, GATT Doc. 1982L/5424 (1982), online: WTO <http://docsonline.wto.org/gen_search/asp> at 2 [emphasis added].

²⁷² *Ibid.* at 9.

²⁷³ There were twenty-one cases of agricultural subsidies during the GATT years. Ten cases were not fully satisfied because there was no decision and eleven were decided. The nine GATT cases studied in this session were chosen for a qualitative study because the decisions examined some concepts such as “more than an equitable share” and

subsidizing practices were inconsistent with the *GATT 1947* rules and condemned those contracting parties that were subsidizing. There was fierce criticism of the vague definitions of *GATT 1947* expressions, such as “equitable share.” However, this problem was not insoluble, because several GATT panels were successfully able to declare that agricultural subsidy practices violated *GATT 1947* Article XVI.

The Tokyo Round Subsidies Code succeeded in defining procedural rules more clearly, especially for countervailing duties, but it did not bring about significant advances in substantive rules. Actually, it raised the threshold to challenge agricultural subsidies and, for this reason, in terms of the challengeability of agricultural subsidies, it did not contribute to trade liberalization on agriculture.

As was seen, the association of “displacement” with the concept of “equitable share” by the TRSC changed the interpretation of this concept during the GATT years. Prior to the TRSC, “equitable share” meant a “share in ‘world’ export trade of a particular product,” but after the implementation of the Subsidies Code, the interpretation of the same concept changed to “trade in that product in individual markets.” Because it is a highly complex task to verify displacement in each importing market, condemnation of agricultural exports subsidies under *GATT 1947* Art. XVI:3 became more complex.

The proof is that the panels²⁷⁴ that addressed the concept of “equitable share” after the Tokyo Round declared that they were able to identify artificial levels of subsidies inconsistent with the TRSC provisions that caused harmful effects to Members. However, they were not able to declare that such subsidies had given to the subsidizing Member “more than an equitable share

“displacement” which evolved during the three phases examined in this research. Therefore, they are important for an evaluation of how challengeability of agricultural subsidies evolved during these phases. See n. 17.

²⁷⁴ *EEC – Pasta Subsidies supra* note 163 and *EEC – Wheat Flour Subsidies supra* note 54.

of the world export trade” in the subsidized product. Sometimes, the panels had difficulties in implementing the new market-effect concepts brought about by the TRSC.

The fact that there were high levels of agricultural subsidization during the GATT years could not be credited to some purported weaknesses or to a hypothetical lack of clarity or complexity of some *GATT 1947* substantive or procedural provisions, as some authors have suggested.²⁷⁵

²⁷⁶ All the panel decisions analyzed in this first part of this study proved that GATT substantive rules were not favorable to agricultural subsidization. One of the most significant problems during the GATT years was compliance, which is a common problem of any international dispute settlement system. This is the reason that the US waiver may have harmed the GATT system, perhaps to a higher degree than any vague provision. It affected compliance and, as a consequence, the credibility of the *GATT 1947* dispute settlement system. Even so, the *Canada – Eggs* case proved that the US might have not received all the benefits it thought it would under the waiver. Through the analysis of several *GATT 1947* provisions and cases, we have seen that a legally consistent framework of substantive rules was created that limited agricultural subsidization.

²⁷⁵ Gary Horlick, for example, states that the GATT dispute settlement system was weak. He was referring particularly to procedural rules of the GATT on compliance and comparing GATT and WTO dispute settlement systems. The GATT dispute settlement system allowed the respondent to impede the implementation of the decision of the panel, and the WTO did not have such a provision. The goal of this research is not to compare procedural regulations as a measure of efficiency between the WTO and GATT. The reason is that they are not two separate systems, because the GATT was the predecessor of the WTO, and both systems demonstrated problems in enforcing the decisions of their respective dispute settlement systems, as is going to be seen next in Chapter II. The research in Chapter I proved through analysis of substantive provisions and GATT cases that agricultural subsidies were consistently condemned during the GATT years. See *infra* note 297.

²⁷⁶ According to Hudec there were 21 (twenty one) cases of agricultural subsidies during the GATT years. According to his criteria 11 (eleven) were partially or fully satisfied and 10 (ten) did not reach any decision. Even though the analysis of this research is not quantitative, 9 (nine) cases that had a decision were analyzed in this part of the study and the substantive ruling of all them were not favorable to agricultural subsidization. See *supra* note 17.

I.6.1 Challengeability of Agricultural Subsidies Before the Peace Clause (GATT Legal Framework)

Therefore, through the analysis of the GATT agricultural subsidies legal framework and through the examination of several cases, the following organizational diagram of *GATT 1947* agricultural subsidies' challengeability was designed, in order to summarize the inherent legal structure.

Table 3: Challengeability of Agricultural Subsidies before the Expiry of the Peace Clause

AGRICULTURE	<i>GATT 1947</i> Art XVI	<i>GATT 1947</i> Art. VI	NV N or I (<i>GATT 1947</i> Art. II and XXIII 1(b))	<i>GATT 1947</i> Art III
Domestic Subsidies	Yes, consultations if cause serious prejudice ²⁷⁷	Yes	Yes	Yes, if not according to (8b) ²⁷⁸
Export Subsidies	Yes, if more than equitable share ²⁷⁹	Yes	Yes	Yes

This diagram shows that agricultural domestic subsidies could be challenged under *GATT 1947* Article XVI, because it stated that, if the subsidies caused serious prejudice, contracting parties could discuss the possibility of limiting subsidization; therefore, domestic subsidization was not an authorized practice if it caused serious prejudice. This shows that export subsidies

²⁷⁷ Art. XVI established consultations to possibly limit subsidization if it is harming another Contracting Party. Because of the possibility of consultation under Art. XVI in GATT, the more correct answer for challengeability of domestic subsidies under *GATT 1947* Art. XVI is yes.

²⁷⁸ The exception of *GATT 1947* III 8(b) did not mean that the authorized subsidies under *GATT 1947* III 8(b) could not be challenged. On agriculture, a country could apply *GATT 1947* Art. III to challenge agricultural subsidies that involved an expenditure of revenue by a government, given exclusively to domestic products. Also, paragraph 9 established that the provisions of Article III could have prejudicial effects on the interests of exporting countries; therefore, any measure taken under Art. III should be taken "with a view to avoiding to the fullest practicable extent such prejudicial effects." At any rate, if the harmed exporting country had a benefit nullified or impaired, it could challenge the measure of the other contracting party under *GATT 1947* Art. XXIII 1(b). The allegation would be that the modification of the commitment on the schedule of concession of the other contracting party conflicted with the provision of *GATT 1947* art. III.

²⁷⁹ *France – Wheat Exports* supra note 64, *EC – Sugar Export (Australia)* supra note 54 and *EC – Sugar Export (Brazil)* supra note 54.

could be challenged, but only if the subsidizing country gained more than an equitable share of the market of the subsidized product. Furthermore, both types of subsidies could be subject to countervailing measures.

Regarding the “nullification and impairment” doctrine (*GATT 1947* Art. II and XXIII), we saw in the *EEC – Canned Fruits*²⁸⁰ and the *EC – Oilseeds* cases²⁸¹ that the respondents tried to allege that nullification or impairment in terms of Article XXIII:1(b) could not be used to challenge agricultural subsidies with an impact on exports. According to them, this type of subsidy had to be exclusively regulated by *GATT 1947* Article XVI, which required displacement of exports to prove adverse effects caused by subsidies. Their allegation can be considered an indication that *GATT 1947* Art. XXIII 1(b) had a lower threshold of challengeability than the market-effect requirement of *GATT 1947* Art. XVI of “more than an equitable share.” At any rate, both types of agricultural subsidies (domestic and export) were challengeable under Article *GATT 1947* XXIII 1(b).

The GATT legal framework did restrict the use of domestic subsidies, because, as was seen, subsidies to domestic producers could be a violation of the national treatment obligation,²⁸² which required equal treatment of foreign and domestic goods with respect to all internal regulatory measures. However, as can be seen in the diagram and in the cases analyzed, *GATT 1947* Article III:8(b) contained an exception from the national treatment obligation; it allowed governments to grant subsidies directly to domestic producers. However, these subsidies had to involve an expenditure of revenue by a government,²⁸³ which did not include tax exemptions.²⁸⁴ At any rate, these subsidies were challengeable under the *GATT 1947*, as indicated in the

²⁸⁰ *EEC – Canned Fruits supra* note 228.

²⁸¹ *EEC - Oilseeds I supra* note 54.

²⁸² See *GATT 1947* Art. III.

²⁸³ *Canada – Periodicals supra* note 223.

²⁸⁴ *Indonesia – Autos supra* note 234 at para. 14.113.

diagram,²⁸⁵ because this exception did not mean that the authorized subsidies under *GATT 1947* III 8(b) could not be challenged. On agriculture, a country could apply *GATT 1947* Art. III to challenge agricultural subsidies that involved an expenditure of revenue by a government exclusively for domestic products.

Moreover, Art. III, paragraph 9, recognized the harmful effects of domestic subsidies. It established that “internal maximum price control measures” could have prejudicial effects to the interests of exporting countries; therefore, any measure taken under Art. III had to be taken “with a view to avoiding to the fullest practicable extent such prejudicial effects.” At any rate, if the harmed exporting country had a benefit nullified or impaired, it could challenge the measure of the other contracting party under *GATT 1947* Art. XXIII 1(b). The allegation would be that the modification of the commitment on the schedule of concession of the other contracting party conflicted with the provision of *GATT 1947* art. III.

²⁸⁵ Specifically, subsidies that do not involve expenditure of revenue by a government, tax exemptions and indirect subsidies, which are subsidies involving payment to persons other than producers themselves, were not protected by the exception of III:8(b). This theory was proved in *EEC - Oilseeds I supra* note 54 and in *Canada – Periodicals supra* note 223.

CHAPTER II

THE LEGAL REGIME FOR AGRICULTURAL SUBSIDIES—THE URUGUAY ROUND

As discussed in Chapter I, this research aims at demonstrating that the expiry of AoA Art. 13 made agricultural subsidies more vulnerable to legal challenges and at describing the new legal boundaries for challengeability after the expiry of the Peace Clause. For that purpose, a comparative analysis should be made of the legal framework for the challengeability of agricultural subsidies at three moments of regulation: during the GATT years, during the WTO years before the expiry of the Peace Clause and during the WTO years after the expiry.

Chapter II analyzes the legal framework of the challengeability of agricultural subsidies during the WTO years prior to the expiry of the Peace Clause and demonstrates that the more complex rules and the rationale of the panels in applying such rules did not necessarily mean a step forward towards trade liberalization.²⁸⁶ The first reason for this was the shield of the Peace Clause, which deflected most of the challenges during the Peace Clause years. The second reason was the market-effect requirements for the challengeability of agricultural subsidization introduced by the TRSC and incorporated by the *SCM Agreement*, which imposed higher thresholds for challengeability.

Complex provisions for challengeability do not necessarily mean a step backwards from trade liberalization, because they could help to identify desirable and non-desirable subsidies.

²⁸⁶ Trade liberalization in the meaning established in the Marrakesh Agreement, which that stated that “[t]hey believe that the trade liberalization and strengthened rules achieved in the Uruguay Round will lead to a progressively more open world trading environment.” *Marrakesh Declaration of 15 April 1994. WTO Legal Texts supra* note 1 at iv [*The Marrakesh Declaration*]

Also, a trade system free of subsidies would not be the best scenario, if we take into account that some subsidies are desirable, because they can foster development, compensate for social disparities and help regions and people in need.

To examine these issues, subsidies have to be divided or classified according to the *SCM Agreement*. Under this Agreement, there are basically three types of subsidies: prohibited subsidies, actionable subsidies (*SCM Agreement* Part III) and non-actionable subsidies. The WTO system has already classified the desirable and the non-desirable subsidies. The subsidies that are prohibited under Part II of the *SCM Agreement* are mainly export subsidies or support programs that are “contingent upon the use of domestic over imported goods,” according to the wording of *SCM Agreement* Art. 3.1. These subsidies have a high potential to distort trade.

Actionable subsidies are, specifically, three types of subsidies that may cause adverse effects, serious prejudice or injury. Later in this study, each type of subsidy and its effects will be examined more closely, but it is relevant to state here that they might or might not distort trade according to their effects on other Members. When such subsidies are challenged under the WTO dispute settlement system, the panel and the Appellate Body verify whether these subsidies caused any harm, what was the extension of this prejudice and the causality involved were. Besides, if the actionable subsidy did not cause any harm, it would not have been challenged, because there would not have been any party interested in doing so.

Non-actionable subsidies do not cause any harm or are classified as such by the WTO for social, educational, political or any other reason that the s agree on in order to declare such subsidies as non-actionable. *SCM Agreement* Part IV, which classified these subsidies, expired in 1999; however, the AoA has a list of subsidies that cannot be actionable (Annex II).

Therefore, the subsidies that can be actionable are basically classified under the WTO rules as potentially trade distortive subsidies. So, this is the reason that such subsidies do not contribute to trade liberalization. Several types of subsidies are not only desirable, but they are also necessary, and they must not be challenged under the WTO rules. Therefore, according to WTO principles, highly complex procedural rules to challenge trade distortive subsidies do not contribute to trade liberalization. There are studies that prove that agricultural subsidization does not only harm poor countries but also the whole international community.²⁸⁷

Chapter II focuses especially on the AoA and *SCM Agreement*, which shaped the boundaries of the challengeability of agricultural subsidies before the expiry of the Peace Clause. It will include an analysis of the Agricultural Modalities and how they are calculated, and the three basic pillars of agricultural regulation: market access, domestic support and export subsidies. It will also analyze the AoA's classification of agricultural subsidies into "boxes": green, non-green and export subsidies. For this purpose, the transition from the GATT to the WTO must be scrutinized.

II.1 The Transition from the GATT to the WTO

The transition from the GATT and the WTO is a continuous and dynamic process. The two cannot be viewed as separate regulatory systems. The relation is continuous, because the WTO continued the GATT's process of agricultural subsidy regulation, in accordance with the

²⁸⁷“Substantial reductions in industrial country agricultural support are therefore important not only for the direct benefits generated for the many economies that are (potential) net exporters but also for the support of efforts by developing country governments to pursue domestic reforms and thus to reap significant gains from the current WTO negotiations on agriculture.” Hoekman, Bernard, Ng, Francis & Olarreaga, Marcelo. *The Impact of Agricultural Support Policies in Developing Countries*. (Washington D.C.: the World Bank, 2007) at 128.

changes that the GATT suffered over the years. It is dynamic, because the GATT is still valid and still has challengeable provisions that can be brought under the WTO dispute settlement system. The current *GATT Agreement (GATT 1994)* comprises the provisions of *GATT 1947* – as modified by the terms of the legal instruments that entered into force before the implementation of the WTO along with other provisions, protocols, explanatory notes and observations specified in the preamble of *GATT 1994*.

In the preamble of the WTO/GATT Declaration on the Uruguay Round²⁸⁸ (Declaration of September 20, 1986), also known as the “Punta Del Este Declaration,” the CONTRACTING PARTIES, at a ministerial level, determined to “preserve the basic principles and to further the objectives of the GATT.” In the four objectives set by the declaration, the GATT was mentioned four times. The goals of the declaration included the need to “strengthen the role of GATT, improve the multilateral trading system based on the principles and rules of the GATT”²⁸⁹ and to “increase the responsiveness of the GATT system to the evolving international economic environment, through facilitating necessary structural adjustment, enhancing the relationship of the GATT with the relevant international organizations.”²⁹⁰

The Uruguay Round was taking place in part to corroborate provisions of the GATT, but also to strengthen the system. An analysis of the declarations emanating from the ministerial meetings that established the creation of the WTO makes clear that the GATT was not to be considered a separate system from the WTO. Rather, the establishment of the WTO was a natural progression, building on the previous GATT and designed to strengthen the system, not to replace it.

²⁸⁸ GATT, *Ministerial Declaration on the Uruguay Round (MIN.DEC)*, adopted in Punta del Este, Uruguay, on 20 September 1986, reproduced in *GATT Focus Newsletter*, No. 41 (1986), online: WTO <http://docsonline.wto.org/gen_search/asp> [*Punta del Este Declaration*].

²⁸⁹ *Ibid.* at para A(ii).

²⁹⁰ *Ibid.* at para A(iii).

In fact, the Punta del Este Declaration determined that the negotiations in the Uruguay Round could not “take any trade restrictive or distorting measure in the legitimate exercise of its GATT rights, that would go beyond that which is necessary to remedy specific situations, as provided for in the General Agreement.”²⁹¹ This proves that the GATT established the limits of challengeability for the agreements resulting from the Uruguay Round.

The Marrakesh Declaration of April 15 1994 formally concluded the Uruguay Round and the Marrakesh Agreements Establishing the World Trade Organization formally established the WTO. The first mentioned that the ministers recognized the need for strengthening not only the GATT but also the WTO to provide technical assistance in their areas of competence.²⁹² It made clear that the GATT was still valid and could be strengthened, as could the WTO, and stated that there was a transition that should be addressed.²⁹³ Therefore, it is clear in the declaration that the *GATT 1947* started the process of regulation, which was continued by the WTO after the Uruguay Round.

However, scholars make the common mistake of comparing the GATT with the WTO as if they were two separate systems. As a result, they disregard the ordinary maturing process that shaped both systems. When they make this judgment, they have the tendency to declare, for example, that the GATT dispute settlement system was flawed, because it had problems with compliance. However, this analysis does not take into account the difference between substantive and procedural rules. Besides, compliance is not only a GATT problem; it is a difficulty inherent to any international dispute system.

²⁹¹ *Ibid.* at para C (ii).

²⁹² *Marrakesh Declaration of 15 April 1994. WTO Legal Texts supra* note 1 at iii [*The Marrakesh Declaration*] and *Marrakesh Agreement Establishing the World Trade Organization, WTO Legal Texts supra* note 1 at 3 [*The Marrakesh Agreement*].

²⁹³ *The Marrakesh Declaration Ibid.* at para. 6.

According to legal dictionaries, substantive rules of law define rights and duties, while procedural rules of law provide the resources to enforce those rights and duties.²⁹⁴ The more advanced and elaborate WTO procedural rules, especially on dispute settlement and countervailing duties, do not mean that GATT substantive rules were flawed.

It is clear that the GATT procedural rules for the dispute settlement system were considerably less elaborate than those of the WTO. Any Member could block compliance with panel decisions. Besides the positive consensus rule, GATT dispute settlement rules had no fixed timetables, and several cases were inconclusively settled in terms of compliance. However, this study is focused on substantive (subject matter) rules and not on procedural rules. It evaluates the legal provisions and the material aspects – the legal reasoning – behind the decisions. If it analyzed the procedural rules, then it would have to go through an analysis of compliance and other procedural aspects of the dispute settlement systems in the GATT and WTO, which are not within the scope of this study.

Besides, more elaborate procedural rules do not necessarily mean that the system that applies them is better. As an example, it is consensus that the TRSC brought about considerable advances in terms of procedural rules, especially for antidumping and countervailing duties. However, the WTO conducted empirical research and found that decisions were blocked more often in the GATT years after the establishment of the TRSC than before it.²⁹⁵ This conclusion means that Members did not always block consensus decisions to allow disputes to proceed,

²⁹⁴ “Substantive law and procedural law are the two main categories within the law. Substantive law refers to the body of rules that determine the rights and obligations of individuals and collective bodies. Procedural law is the body of legal rules that govern the process for determining the rights of parties.” Gale Group. *West’s Encyclopedia of American Law*. (Eagan: West Group Publishing, 1998). Substantive law defines rights and duties and procedural law provides the tool to enforce them.

²⁹⁵ WTO, *Historic Development of WTO Dispute Settlement System*, online: WTO <http://www.wto.org/english/tratop_e/dispu_e/dispu_settlement_cbt_e/c2s1p1_e.htm>

even if this was against their short-term interests. The fact that a veto could be used in the future against the country that used it in the present helped to prevent constant blocks.

According to the same WTO study, it was determined that the solutions that the GATT dispute settlement system resulted in satisfied the parties in most of the cases. The study did not cover the disputes that were not brought forward. There is no data to indicate how many disputes were not brought forward because one contracting party concluded that the effort was not worthwhile, since the other contracting party could block the panel. Besides, as stated, there are some important differences with respect to the establishment of panels, adoption of panel reports and authorization of suspension of concessions. Many commentators agree that the WTO system, while not perfect, is more effective and binding than the GATT system, and it is more likely to induce compliance. This corroborates the statement above and confirms that the WTO dispute settlement system is more elaborate, and for this reason, it could be more effective in terms of compliance and procedural rules.

However, a qualitative analysis of GATT cases identified, that during these years, there was a legal rationale to limit agricultural subsidies. And this conclusion is not based on an analysis of procedural rules or of dispute settlement systems or even on a quantitative analysis of compliance. This conclusion is based exclusively on a qualitative analysis of substantive rules. Therefore, it should be clarified here that this study does not conclude that the GATT system was more efficient than the WTO system. It was not. A qualitative analysis of legal provisions and cases showed that, during the GATT years, there was a legal rationale based on simple material rules to limit agricultural subsidies.

The evidence for such conclusion was found in the *GATT 1947* cases and legislation analyzed in the first chapter that concluded that after the implementation of the TRSC panels

were more blocked than during the *GATT 1994* years. Besides, the same study proved that the solutions provided by the *GATT 1947* dispute settlement system used to satisfy the contracting parties. The same satisfaction does not occur under the WTO dispute settlement system.²⁹⁶

Gary Horlick²⁹⁷ compared dispute settlement during the GATT and WTO years and found that there were not many cases challenging subsidies under the TRSC provisions. One possible reason for the stillness of the TRSC dispute settlement system, according to Horlick, was the “glass house” principle, whereby governments that live in glass houses (i.e., give their own subsidies) do not throw stones at others.

It is relevant to remember, however, that the TRSC was not signed by all of the GATT contracting parties, and it was agreed to in 1979, long after the *GATT 1947* had been created, in 1947. These reasons certainly contributed to the fact that the Code was not constantly used in GATT disputes. Besides, if the TRSC system of dispute settlement was not frequently used for reasons of legal inaccuracies, then the *SCM Agreement* purportedly would have the same problem, because, as was seen above, its system of dispute settlement is very similar to and is based on the TRSC.

Furthermore, comparing the number of GATT subsidy cases under the TRSC to the number of the WTO subsidy disputes is a not an appropriate exercise, to say the least. The number of provisions in the WTO legal framework is significantly higher.²⁹⁸ Besides, the GATT is the basis of the whole WTO system and as has been seen, its regulation of dispute

²⁹⁶ WTO, *Diagnosis of the Problems Affecting the Dispute Settlement Mechanism*, WTO Doc. TN/DS/W/90 (2007), online: WTO <http://docsonline.wto.org/gen_search.asp>.

²⁹⁷ Horlick, Gary, “John Jackson and the Development of GATT/WTO Subsidies Rules” in Bronckers, Marco. & Quick, Reinhard. eds., *New Directions in International Economic Law: Essays in Honour of John H. Jackson* (The Hague: Kluwer Law International, 2000) at 259.

²⁹⁸ Almost 300 cases had been brought to the Dispute Settlement Body and the Cancun Ministerial Conference up to 2003, which can be compared with the final total of 300 cases filed during the entire 47 years of the former GATT. WTO, *Cancun WTO Ministerial 2003: Briefing Notes*, online: WTO <http://www.wto.org/english/thewto_e/minist_e/min03_e/brief_e/brief13_e.htm>.

settlement,²⁹⁹ which evolved over the years, built the foundation for most of the WTO DSU provisions.

Some scholars criticize the GATT's rudimentary system when comparing it with the WTO's. However, the GATT dispute settlement system established under Arts. XXII and XXIII in 1947 can be considered a significant evolution in terms of dispute settlement, especially if compared with other international dispute settlement systems of that time. The statutes of the Permanent Court of International Justice created in 1922 did not have a provision providing a remedy for any violation of international statutes brought before the Court, nor did its successor, the statute of the International Court of Justice annexed to the Charter of the United Nations.³⁰⁰ The statute established suspension of concessions as a remedy for a possible violation of the GATT. The same remedy was used later by the WTO DSU.

In reality, the *GATT 1947* dispute settlement system began with two provisions, but it substantially evolved over the years to a more complex set of regulations through the creation of several procedural rules to regulate dispute settlement. First, contracting parties themselves had to resolve the matter. Later, disputes that were decided by rules of the Chairman of the GATT Council evolved into the so-called working parties composed of representatives of all interested CONTRACTING PARTIES, which included the parties involved in the dispute that could block the decision. Panels with three or five independent experts that could not be linked with the countries in the dispute defined the last GATT system to settle disputes. Independent panel

²⁹⁹ Especially the following decisions: GATT, *Decision of 5 April 1966 on Procedures under Article XXIII*, 14th Supp. B.I.S.D. (1966) 18 online: WTO <<http://docsonline.wto.org/gen. search/asp>> [*GATT Decision on Procedures 1966*]; GATT, *The Understanding on Notification, Consultation, Dispute Settlement and Surveillance*, 26th Supp. B.I.S.D. (1979) 210 online: WTO <<http://docsonline.wto.org/gen. search/asp>>; GATT, *The Decision on Dispute Settlement, contained in the Ministerial Declaration*, 29th B.I.S.D. (1982) 13 online: WTO <<http://docsonline.wto.org/gen. search/asp>>; GATT, *The Decision on Dispute Settlement of 30 November 1984*, 31st B.I.S.D. (1984) 9. online: WTO <<http://docsonline.wto.org/gen. search/asp>>.

³⁰⁰ See Taslim O. Elias, *The International Court of Justice and Some Contemporary Problems : Essays on International Law* (Boston: Kluwer Boston, 1983).

reports were written with recommendations and rules to settle the disputes. After the approval of the GATT Council, the report was binding.³⁰¹

It can be noted that, even though GATT procedures for dispute settlement were simpler and less rule oriented,³⁰² a dispute had to be resolved in a shorter time, and its provisions were the basis of several DSU articles that defined the WTO dispute settlement system. However, as stated, in the GATT system, the party that had lost the dispute could block the implementation of the panel decisions. Besides the positive consensus rule, the GATT dispute settlement system did not have as many fixed deadlines as the WTO system, and many cases were inconclusive in terms of compliance.

That is the reason that Horlick also stated that the GATT dispute settlement system was “weak,” particularly because of the possibility for the respondent to block³⁰³ any panel decision. According to him, this certainly did not encourage governments to bring forward complaints about subsidies. It seems that Horlick was not only comparing the two systems (GATT and WTO) but was also making the comparison as if the GATT and the WTO were very distinct systems of subsidy regulation. As was stated, the WTO could not exist if the GATT had not been its predecessor.

Horlick went on to quote some GATT disputes whose decisions were not complied with for non-legal reasons³⁰⁴ and stated that the result was discouraging because some panel reports were not adopted. In his opinion, the doctrine of nullification and impairment was not strong enough. Some cases he mentioned have been analyzed in the first part of this study, and they made a consistent legal analysis of the problem and condemned agricultural subsidies. As stated

³⁰¹ *GATT Decision on Procedures 1966 supra* note 299 at para. 5.

³⁰² See *supra* note 265.

³⁰³ The GATT Dispute Settlement System allowed the respondent to impede the implementation of the decision of the panel.

³⁰⁴ *EEC – Oilseeds I supra* note 54 and *EEC – Wheat Flour Subsidies supra* note 54.

before, the WTO dispute settlement system also has compliance problems, and the *SCM Agreement* dispute system for prohibited and actionable subsidies was based on the TRSC established during the GATT years.

The main weaknesses of the WTO dispute settlement system are, among others, lack of transparency,³⁰⁵ high cost of litigation and, especially, lack of compliance. In order to try to resolve this problem, the DSU has established three different possible procedures to try to make Members comply with the decisions. The first one is established in DSU Art. 21.3(c), which provides for arbitration to define a reasonable period of time for compliance with recommendations for compliance. The suggestion is around 15 months. The second possibility is Art. 21.5, which establishes another panel to make a decision whenever there is a disagreement about compliance with the recommendations of the main panel. Basically, 21.5 procedures mean another panel. The DSU suggests that the report be issued in 90 days; however, the dispute can take longer. The third possibility is regulated by DSU Art. 22.6 and occurs when the levels of the suspension of concessions or its principals and procedures are objected to. In this case, the DSU suggests arbitration conducted by the original panel or by an arbitrator appointed by the Director-General. The procedures should last 60 days or a reasonable period of time.

With the DSU providing possibilities to review a decision, they can be delayed and non-compliance is considered an important problem of the WTO dispute settlement system.³⁰⁶ Forty one (41) cases³⁰⁷ have been brought under DSU Art. 21.5, which means that Members are struggling with compliance. The *US – Upland Cotton*³⁰⁸ case is an example. It started seven

³⁰⁵ Bernard M. Hoekman & Petros Mavroidis, “WTO Dispute Settlement, Transparency and Surveillance” (2000) 23 *World Economy* 527.

³⁰⁶ See *supra* note 296. For an assessment of the current system of WTO dispute settlement see Annex I.

³⁰⁷ WTL, *List of all WTO complaints brought pursuant to DSU Article 21.5*, online: WTL <<http://www.worldtradelaw.net/history/urdsu/urdsu.htm>> at 1-7.

³⁰⁸ *US – Upland Cotton* *supra* note 14.

years ago and has still not been complied with. In this case, as in many others, legislative action to change national statutes was necessary, which makes compliance even more difficult.

Both the GATT and the WTO systems had problems with compliance. The WTO has a significantly more elaborate dispute settlement system and procedural rules. Consequently, it is supposed to have a more efficient system in terms of compliance; however, the complexity of the system has also established possibilities to circumvent compliance, which is the cause of the serious compliance problems described above.

The political interference that happened during the GATT years is also commonly considered as another flaw of the GATT system. Political (or any other non-legal) interference is also a factor in other international systems. Actually, it can be said that all the non-legal interference in the GATT helped to build a better system. Furthermore, the WTO dispute settlement system is not free from non-legal interference either. The analysis of the WTO system regarding challengeability of agricultural subsidies will demonstrate that one system is no better than the other and the WTO raises the threshold for challengeability of agricultural subsidies, as the analysis of the treatment of agriculture in the WTO will show.

II.2 Agriculture in the WTO System

The creation of the WTO, and its regulatory system implemented in 1995 at the end of the Uruguay Round [UR], entrenched a new and more complex regime to discipline the use of subsidies. The *SCM Agreement* strengthened the subsidies' legal regime and imposed higher standards to challenge agricultural subsidization under the WTO system.

The Uruguay Round essentially changed the way that agriculture was treated under the *GATT 1994*. As such, it can be considered a turning point in the construction of agricultural policy. WTO Members consensually agreed to a set of principles and regulations that aimed at reducing trade distortions caused by GATT agricultural policies. The goal was to reduce agriculture trade distortions such as quotas, minimum import prices, high import rates and others. As is going to be seen in this chapter, there is evidence that these goals have not been achieved so far.

The *AoA* was created under the justification that it was necessary to establish a more equitable and less trade-distortive agricultural trading system through consistent and steady reductions in agricultural measures of support and protection. It regulates specific binding commitments by WTO Members to improve market access and to reduce export and domestic trade-distortive subsidies. It is beyond the scope of this study to evaluate whether the WTO has established a more equitable agricultural trading system.³⁰⁹ However, it will be shown in this chapter that, from a legal perspective, the WTO system not only gave agriculture special status, but it also raised the standards for legal challenges of agricultural subsidies.

The creation of the *AoA* was fostered by the need to reduce production surpluses during the 1980s and 1990s, caused by high levels of support and protection. During these years, the amount of subsidies was significantly high, especially in the US and the EC.

Purportedly agreeing to limit those subsidies and reduce import barriers, WTO Members aimed at reducing support policy spending and ending the devaluation of world's commodity prices. The impact of *AoA* trade liberalization was supposed to be an expansion of market access and a reduction in distortions in trade consumption and production.

³⁰⁹ For this purpose see Stefan Tangermann, "Has the Uruguay Round *Agreement on Agriculture* Worked Well?" *working paper # 01-1, 2001* (Minnesota: International Agricultural Trade Research Consortium, 2001) [Tangermann, "Has the UR worked well?"].

The preamble of the *AoA* established that the goal of the Agreement was to set a “fair and market oriented agricultural trading system and that a reform process should be initiated through the negotiation of commitments on support and protections and through the establishment of strengthened and more operationally effective *GATT 1994* rules and disciplines.”³¹⁰ Taking into account the high level of agricultural subsidies used in the present day, it seems that these goals of the *AoA* have not been not achieved.

Furthermore, the *AoA* preamble mentioned that it was in line with the “Punta del Este Declaration,”³¹¹ which, as quoted before, stated that the Uruguay Round and its Agreements should “further the objectives of GATT.”³¹² It seems that the declaration was mentioned to further the objectives of agricultural trade liberalization, which are one of the main reasons both the GATT and the WTO were created. But if agriculture gains a special status, thereby making challengeability more difficult, it is not clear whether the *AoA* is, in fact, furthering the objectives of the GATT .

In the *GATT 1947* framework, the regulations were the same for both agricultural and industrial subsidies. The same regulation could mean agriculture was less distorted, despite the exceptions in *GATT 1947* Articles XVI and XI. Whether or not the *AoA* really does reduce these distortions is a question that remains open. However, undoubtedly, the *AoA* has given agriculture a special status, because it separated the regulation of the two types of subsidies, as is going to be analyzed in the next section.

³¹⁰ See *AoA*, preamble at para. 2.

³¹¹ *Ibid* at para. 1.

³¹² *Punta del Este Declaration supra* note 288.

II.3 The Agreement on Agriculture [AoA]

The AoA defined new rules for agriculture, shaping the legal framework for agricultural subsidies. Some scholars³¹³ asked whether it was necessary to make rules for agriculture more specific, mainly because it had always escaped the regulations that worked reasonably well in other sectors of international trade. Given that the regulation of agriculture was set apart in the *GATT 1947* system in Articles XVI and XI and became highly distorted, it would have made sense, therefore, for the Uruguay Round to have made agricultural regulations less “special” and, as a result, less distorted. However, that did not happen because of, among other reasons, the shield of the Peace Clause.

II.3.1 The Peace Clause

Agriculture was not only a major topic at Doha, but also a relevant theme during the Uruguay Round negotiations in 1994. The *Agreement on Agriculture* subjects agricultural subsidies to a more specific set of rules than those applicable to industrial subsidies. The Peace Clause was one of the measures used to bring this about.

II.3.1.1 The Background of the Peace Clause

During the Uruguay Round negotiations, the two leading forces—the US and the EC—could not reach an agreement over export subsidies. The US called for a “complete phase out

³¹³ Tim Josling; Stefan Tangermann, and T. K. Warley, *Agriculture in the GATT : Past, Present and the Future*, (Lond: Macmillan, 1996) [Josling, *Agriculture in the GATT*].

over ten years of all agricultural subsidies which directly or indirectly affect trade.”³¹⁴ The EC insisted on a progressive reduction without any determined timetable.³¹⁵ The divergent positions resulted in a delay in negotiations until the US stepped back from its idea of “eliminating all trade distortions” and accepted a less ambitious goal of “substantial progressive reductions in agricultural support and protection sustained over an agreed period of time.”³¹⁶

Aart De Zeeuw, chairman of the negotiating group on agriculture, tried to expedite the negotiations and presented a draft in 1990, aimed at consolidating the positions of the US and the EC. He proposed that subsidies continued to exist but with substantial reductions compared with other forms of protection. However, he did not suggest any concrete figure;³¹⁷ therefore, once again, the US and the EC did not reach an agreement.

A new proposal, dubbed Dunkel Draft, was put on the table by the WTO Director-General in the Draft Final Act of December 1991 and suggested cutting export subsidies by 24%. The EC did not agree with this, because the proposal limited the amount of export subsidies. This deadlock in negotiations led to a series of negotiations concluded in November 1992 with the Blair House Accord.³¹⁸

The Blair House Accord modified the terms of the Dunkel Draft on agriculture. Due to insistence on the part of the EC, the export subsidy quantity reduction was scaled down from 24% to 21%, and the Aggregate Measurement of Support [AMS] (the total amount of support

³¹⁴ Croome, John, *Reshaping the World Trading System: A History of the Uruguay Round* (Geneva: Aspen Publishers, 1995) at 114.

³¹⁵ Terence Stewart, *The GATT Uruguay Round: A negotiating History 1986-1992* (The Hague: Kluwer Law International, 1993) at 179.

³¹⁶ GATT, *Mid-Term Meeting*, GATT Doc. MTN.TNC/11 (1989) online: WTO <<http://docsonline.wto.org/gen.search/asp>>

³¹⁷ A. De Zeeuw, “Implementation and Accomplishments of the WTO, Paper presented at a Seminar organized by the International Policy Council on Agriculture, Food and Trade, in Proceedings of the IPC”. *Proceedings of a Conference Held 13 May 1997* (Washington: IPC, 1997) at 21.

³¹⁸ Hathaway, Dale & Ingco, Merlinda. “Agricultural Liberalization and the Uruguay Round” *paper presented at the World Bank Conference on “The Uruguay Round and the Developing Economies* in Martin, Will & Winters, Alan., *The Uruguay Round and the Developing Countries* (Washington: Cambridge University Press, 1996) at 10 [Hathaway & Ingco, *Agricultural Liberalization*].

measures) commitments on domestic support were modified to apply to an aggregate of all commodities rather than to each individual commodity. It was also agreed that both the EC and the US direct payment programs for cereals would be included in the "blue box" category. The last EC requirement to sign the Agreement was a clause that would shield all forms of agricultural subsidies for a certain period of time, so that producers could have a grace period regarding challengeability during the implementation of the reductions.³¹⁹ For this reason, the Peace Clause was designed.

The Blair House Accord was agreed on between the US and the EC and ended the impasse that threatened the completion of the Uruguay Round. The Peace Clause was used as leverage to make the EC accept the *AoA* provisions and schedules to reduce agricultural subsidies. It could be said that the Peace Clause was agreed upon bilaterally. The EC demanded it in order to agree with the complete package of the Uruguay Round, and the US conceded. Later, the Peace Clause was validated by all WTO Members in the *AoA* with the implementation of the Uruguay Round package of agreements.

This bargaining chip, however, came at a very high cost to the whole international trading community, especially for those countries that exported agricultural products.

II.3.1.2 Substantive Provisions

AoA Art. 13 is called the *Due Restraint* provision, because it has the power to limit the challengeability of agricultural subsidies during the implementation period. *AoA* Art. 1(f) establishes that "for the purposes of Article 13, it [the implementation period] means the nine-

³¹⁹ Josling, *Agriculture in the GATT* *supra* note 313 at 161.

year period commencing in 1995,” which means that the clause expired on December 31, 2003.³²⁰

The expiration of the Peace Clause opened up the possibility of challenging agricultural subsidies under the *SCM Agreement*. As was previously discussed, Art. 13 of the *Agreement on Agriculture* exempts three categories of subsidies from challenges under the *SCM Agreement* (or under the *GATT 1994*).

The first category includes export subsidies “that conform fully to the provisions of Part V of this Agreement [Arts. 8 to 11], as reflected in each Member’s Schedule.” Art. 8 establishes that each Member cannot provide export subsidies if they are not in conformity with *AoA* provisions as specified in the Member’s schedules. Art. 9 determines a *numerus clausus* list of export subsidies subject to reduction commitments under the *AoA*, the methodology, the period of time and the reduction limits of export subsidization, according to the rules and limits in the schedules. *AoA* Art. 10 establishes that no export subsidies authorized under *AoA* Art. 9 according to the limits in the schedules shall be applied in a manner that circumvents any export subsidy commitment and also establishes some limits for international subsidies for food aid. Art. 11 regulates incorporated products.³²¹ The words “conform fully” in *AoA* Art. 13 corroborate the fact that export subsidies should be exclusively limited to the schedules mentioned in Part V.

These subsidies were totally exempt from all challenges under *GATT 1994* Art. XVI and *SCM Agreement* Art. 3, 5 and 6 and could only be challenged by countervailing duties upon

³²⁰ In Panel Report, *Mexico – Definitive Countervailing Measures on Olive Oil* (2008), WTO Doc. WT/DS341/R at para. 7.153 adopted 21 October 2008 [*Mexico – Olive Oil*] the panel decided that “depending on whether ‘years’ are defined as financial or marketing years, the date of expiry of the implementation period might have been some point during 2004.”

³²¹ *AoA* Art. 11 states that “in no case may the per-unit subsidy paid on an incorporated agricultural primary product exceed the per-unit export subsidy that would be payable on exports of the primary product as such.”

determination of injury or threat thereof and if due restraint was exercised. Injury was a requirement for application of countervailing duties. For this reason, in practical terms, the requirement of Art. 13 that export subsidies could be countervailed only “upon a determination of injury or threat thereof based on volume, effect on prices, or consequent impact in accordance with Article VI of *GATT 1994* and Part V of the Subsidies Agreement” avoids the application of provisional measures, because only these measures could be applied to countervail subsidies without definitive proof of injury.

The fact that Art. 13 establishes that injury or threat thereof should be based on volume or effect on prices does not raise the requirements for the challengeability of export subsidies during the Peace Clause years. The reason is that *SCM Agreement* Art. VI, which regulates countervailing duties, had already established that determination of injury had to involve an objective examination of the “volume of the subsidized imports” and the “effect of the subsidized import on prices.” However, the requirement of Art. 13 that due restraint be exercised regarding countervailing duties limited this type of challenge during the peace years.

The concept of due restraint was analyzed in *Mexico – Definitive Countervailing Measures on Olive Oil [Mexico – Olive Oil]* which defined it as a “proper, regular and reasonable demonstration of self-control, caution, prudence and reserve.” The panel also produced objective criteria to identify when due restraint could be found. In this case, Mexico had to demonstrate that it acted with “self-control” and there was no “material retardation.” Initiation with no consultations could not be considered as due restraint.³²² At any rate, this provision made the challengeability of export subsidies—the most distortive trade support measures—significantly difficult during the Peace Clause years, especially because of the limitations on challengeability in *SCM Agreement* Arts. 3, 5 and 6.

³²² *Mexico – Olive Oil supra* note 320 at paras. 7.70-7.79.

SCM Agreement Art. 3 was the main provision in the WTO system designed to avoid subsidies contingent upon export performance, because it established a flat prohibition for this type of trade-distortive measure. If it was not applicable to agricultural subsidies during the Peace Clause period, there was no other way³²³ to challenge these trade-distortive measures except through countervailing duties. The fact that Art. 13(c)(ii) also prohibited challenges of export subsidies under *SCM Agreement* Arts. 5 and 6 demonstrates that, even though export subsidies caused injury to the domestic industry and nullification or impairment of benefits or serious prejudice to the interests of a Member, they could not be challenged.

The other category of subsidies shielded by the Peace Clause was that of domestic support measures regulated under *AoA* Art. 6: amber boxes,³²⁴ which were subject to reduction commitments contained in Part IV of Members' schedules; blue boxes,³²⁵ regulated under paragraph 5; subsidies³²⁶ under *de minimis* levels, regulated by paragraph 4; and subsidies³²⁷ given for poor producers in developing countries, regulated under paragraph 2.

AoA Art. 6 defines amber box subsidies as the domestic measures that support price or are directly related to production quantities. For this reason, they distort trade and do not fall in the category of subsidies that purportedly do not distort trade (green box) regulated under *AoA* Art. 6.1 and Annex II and in the category of blue box regulated under *AoA* Art. 6.5.

³²³ GATT Art. XVI had a less stringent language and *SCM Agreement* Art. 6 regulated serious prejudice to challenges of actionable subsidies; therefore they were subsidiary provisions for export subsidies' challengeability, comparing to the *SCM Agreement* Art. 3.

³²⁴ The so called amber box measures are subsidies regulated under *AoA* Art. 6, excluding green box measures regulated in *AoA* Annex II.

³²⁵ Payments based on fixed area and yields and payments made on 85 per cent or less of the base level of production.

³²⁶ The product-specific or non-product specific support must not exceed 5 per cent of Member's total value of production of a basic agricultural product. The percentage for developing countries is 10 per cent.

³²⁷ This type of subsidy includes support measures available to low-income or resource-poor producers in developing countries to encourage diversification from growing illicit narcotic crops.

Amber box subsidies are subject to reduction commitments according to the schedule of each WTO Member and to *de minimis* levels established by *AoA* Art. 6.4, under which supports are allowed: 5% of product-specific domestic support and non-product-specific domestic support and 10% for developing countries.³²⁸

The blue box subsidies—direct payments under production-limiting programs—are considered as trade distorting but at a lower level if compared with the amber box subsidies related to price support measures. Nevertheless, these payments require farmers to produce in order to be eligible for the payment. Payments may be directly dependent on production as long as the payment is based on a determined area and yields or the volume does not exceed 85% of production in the base period or a livestock payment is based on a fixed number of head.³²⁹ Even though blue box subsidies are related to production, they are not related to the quantity of the production.

These categories of subsidies were exempt from application of countervailing duties unless injury or threat of injury could be proved under *GATT 1994* Art. VI and *SCM Agreement* Part V (Arts. 10 to 23) and due restraint was exercised. The restriction was the same as for export subsidies; however, the language was different. While *AoA* Art. 13(c)(i) established that export subsidies were “subject to countervailing duties only upon a determination of injury ...,” Art. 13(b)(i) determined that domestic support measures were “exempt from the imposition of countervailing duties unless a determination of injury ... was made.” There was an emphasis on

³²⁸ *AoA* Art. 6.4 establishes:

A Member shall not be required to include in the calculation of its current Total AMS and shall not be required to reduce: (i) product specific domestic support which would otherwise be required to be included in a Member’s calculation of its Current AMS where such support does not exceed 5 per cent of that Member’s total value of production of a basic agricultural product during the relevant year; and (ii) non-product specific domestic support which would otherwise be required to be included in a Member’s calculation of its Current AMS where such support does not exceed 5 per cent of the value of that Member’s total agricultural production.

³²⁹ *AoA* Article. 6:5 (a) ii

the limitation of countervailing domestic measures because of the word “exempt,” but in practical terms, the consequences were the same: neither domestic nor export subsidies could be countervailed if there was no proof of injury or threat thereof, and due restraint had to be applied for both.

AoA Art. 13b(ii) established that these domestic support measures were also exempt from actions under *GATT 1994* Art. XVI and *SCM Agreement* Arts. 5 and 6 if not given in excess of that decided during the 1992 marketing year. The meaning of the word “decided” was one of the reasons for the disagreement between Brazil and the US in *US – Upland Cotton*. The US alleged that the word “decided” was in contrast with the word “provided” in some other parts of the *AoA*;³³⁰ therefore, levels of support used as a reference for limitation under *AoA* Art. 13 were the levels decided in 1992 and not those provided in the current year.

According to Brazil, this interpretation would open up the possibility of higher levels of subsidization. The panel ruled on the meaning of the word “decided”: “[c]ome to a determination or resolution ...”³³¹ This was a meaning similar to the one the US was defending. The panel used “decisions made during the 1992 marketing year”³³² as reference to calculate the limits of subsidization and not the levels of subsidies “provided” that year, as Brazil wanted. This meant that the levels of subsidization allowed by the Peace Clause could be even higher than those provided for in 1992.

Amber and blue box subsidies whose challengeability was limited by *AoA* Art. 13(b), differently from export subsidies, were not prohibited by their nature. They had to cause adverse effects in order to be challenged. That was the reason that Art. 13 limited challengeability for

³³⁰ Panel Report, *United States – Subsidies on Upland Cotton*, (2005) WT/DS267/R, Corr.1, and Add.1 to Add.3, at para. 7.425 adopted 21 March 2005, as modified by Appellate Body Report WT/DS267/AB/R, DSR 2005:II, 299 [*US – Upland Cotton*].

³³¹ *Ibid.* at para. 7.434.

³³² *Ibid.* at para. 7.456.

them under *SCM Agreement* Art. 5 and 6 (actionable subsidies) and not under *SCM Agreement* Art. 3 and 4 (prohibited subsidies). Therefore, even if subsidies regulated under *AoA* Art. 6 caused adverse effects through injury, nullification or impairment of benefits accruing directly or indirectly to other Members or serious prejudice, they could neither be actionable nor countervailed, if given under the limits decided in 1992.

The third limitation for challengeability for amber, blue, *de minimis* and low-income subsidies established under *AoA* Art. 13(b)(iii) was that of exemption from challenges based on non-violation nullification or impairment of the benefits of tariff concessions regulated under *GATT 1994* Art. II in the sense of paragraph 1(b) of *GATT 1994* Art. XXIII, if they were not given in excess of what was decided in the marketing year of 1992.

One of the adverse effects established by *SCM Agreement* Art. 5 was nullification or impairment of benefits according to *GATT 1994* Art. II and XXIII 1(b). Therefore, the challengeability of subsidies that nullified or impaired benefits was already indirectly limited through limitation of challengeability under *SCM Agreement* Art. 5 by Art. 13(b)(ii). However, part (b) (iii) limited the challengeability of subsidies that nullified or impaired benefits directly through *GATT 1994* Arts. II and XXIII, so neither the *SCM Agreement* nor the *GATT 1994* could be used as a legal basis for the challengeability of these subsidies during the Peace Clause years.

The last category of subsidies shielded by the Peace Clause was that of green box measures that were supposed to be the less distortive support measures defined as *numerus clausus* in a list in *AoA* Annex II. This category was “non-challengeable,” which means completely exempt from countervailing duties, exempt from actions based on *GATT 1994* Art. XVI and II in the sense of XXIII 1(b) and *SCM Agreement* Part III. There is no case addressing the difference between the terms “exempt” and “non-actionable.” In practical terms, both mean

prohibition and limitation of challengeability according to the terms of the provisions. The fact that green box measures were exempt from *SCM Agreement* Part V means that they could not be challenged, whether or not they would have had an impact on exports.

During the Peace Clause period, there was a free ride for green subsidization. It was supposed to not have distortive effects on other Members, but because of the process of box-shifting, which will be analyzed in the next section, this category completely protected from challengeability distortive subsidies that were not green but were classified as if they were.

II.3.1.3 The Proliferation of Distortive Measures During the Peace Clause Period

The restraint in challengeability brought about by the Peace Clause was one of the main causes of the circumvention of reduction commitments after the Uruguay Round. During the Peace Clause years, distortive measures were put in place with basically no limits,³³³ and there was an escalation in agricultural support measures—legal and illegal.³³⁴ Legal subsidies were given according to the schedules of reductions. Illegal subsidies were given above the schedules' limits or were distorting measures (amber box) classified under a non-distortive category (green box). This process is called box-shifting.

There are studies proving that the subsidies of some heavily agricultural-subsidizing countries have been “greening” over the years.³³⁵ Prior to 1995, the US was preparing for the Uruguay Round; thus, it suffered an amazing process of “greening” distortive agricultural subsidies. “Over the period 1986-1988, programs that would have qualified for green box had

³³³ See Kym Anderson. “The Challenge of Reducing Subsidies and Trade Barriers” *World Bank Policy Research Working Paper 3415, 2004* (Adelaide: WBG-ITU and CEPR, 2004) at table 2 [Anderson, “Reducing Subsidies”].

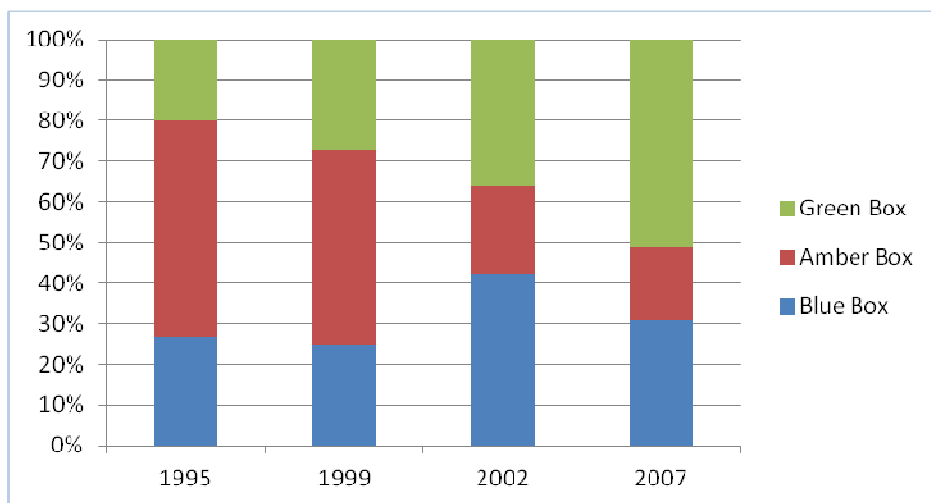
³³⁴ See *Second IDB-CEPII Conference: “Economic Implications of the Doha Development Agenda for Latin American and the Caribbean”* (Sao Paulo: ICONE, 2004) [Jank & Jales, *Blame Shifting*].

³³⁵ *Ibid.*

total expenditures of, on average, just over \$26 billion. From 1996 to 1998, green box spending had increased to an average of \$50 billion.” In 1999, green box subsidies represented around 80 percent of agricultural subsidies declared by the country.³³⁶

The same process occurred in the EC and Japan. Since 1995, amber and blue box expenditures have been retracted considerably, while green box spending has significantly increased. In Japan, green box subsidies rose from 60% in 1995 to almost 80% in 1999. In the EC, the same kind of subsidy rose from 20% in 1995 to approximately 50% in 2007, as can be seen below.³³⁷

**Graphic 1: The Greening Shift of Domestic Support:
EC Notifications at the WTO from 1995 to 2002**



Another problem during the peace years, to circumvent Uruguay Round commitments on agriculture, was “product shifting.” Several mechanisms were applied to give special treatment

³³⁶ Chad E. Hart. & Bruce A. Babcock, “US Farm Policy and the World Trade Organization: How do they match up?” *Card Working Paper 02-WP 294 February 2002* (Aimes, Iowa: 2002) at 11 cited in *Ibid.* at 26.

³³⁷ The source was the Institution of International Trade Negotiations [ICONE] in Jank & Jales, *Blame Shifting supra* note 334 at 25.

to sensitive products as a consequence of tariffication, such as tariff peaks, tariff escalations, specific tariffs, TRQs and special safeguards. These measures were also required by some Members in order for them to accept the *AoA* package negotiated during the Uruguay Round.

These special measures, however, have been used on a very frequent basis and, consequently, have harmed the process of trade liberalization on agriculture. To present one example, according to the table below,³³⁸ powdered milk had very high tariffs with high peaks, tariff-rate-quotas and special safeguards applied by the EEC, the US, Japan, Switzerland and Norway.

**Table 4: Product-Shifting in Market Access:
Tariff Restrictions on Sensitive Agricultural Products in Specific Countries**

PRODUCT	EC	US	JAPAN	SWITZERLAND	NORWAY
Raw Sugar	160.8*	167.0*	154.3*	185.4*	82.0*
Ethyl Alcohol	46.7*	47.5*	83.3	53.2*	424.0*
Powdered Milk	68.4*	49.1*	196.7*	96.2*	552.8*
Poultry Cuts (Frozen)	94.5*	16.9*	11.9	1136.6*	746.3*
Pork (Frozen)	50.6*	0.0	309.5*	211.5*	363.0*
Beef (Frozen)	176.7*	26.4	50.0	698.4*	773.3*
Corn	84.9*	2.3*	95.4*	253.6*	341.0*
Tobacco	24.9*	350.0	0.0	8.6*	0.0
Orange Juice	15.2	44.5*	21.4	31.7*	0.0
<i>Tariff-Rate Quotas</i>	7	4	1	0	6
<i>Specific Tariffs</i>	8	6	4	9	7
<i>Special Safeguards</i>	5	3	2	6	7

The proliferation of trade-distorting measures a consequence of the Peace Clause contributed to making agricultural regulation under the WTO become more a specific and

³³⁸ The source was the Institution of International Trade Negotiations [ICONE] in Jank & Jales, *Blame Shifting supra* note 334 at 21 [The title was modified by the author].

separate discipline in comparison with trade in manufacturing, which goes against the goals of the WTO for agriculture.³³⁹

II.3.2 The Specificity of the *Agreement on Agriculture*

The *AoA* diverges in many significant aspects from the general provisions applicable to trade in manufacturing. It was alleged that some exceptions³⁴⁰ for agriculture in the *GATT 1994* had set agriculture apart from the rest of trade. The Uruguay Round marked the establishment of an official separate Agreement establishing a set of specific rules for agriculture, which included several agricultural schedules determining the quantitative details of the commitments that countries had established and had to comply with under the *AoA*.³⁴¹ In short, agriculture has a much more specific status under the WTO legal framework than it did under the *GATT 1947*.

Certainly, the *AoA* was a historic mark in agricultural regulation. As is going to be verified in the next sections, bound tariffs replaced non-tariff restrictions, and export subsidies were addressed. However, it seems that the Agreement did not move forward as it should have towards trade liberalization in agricultural products. Tariffs on agriculture are still much higher³⁴² as compared with those for industrial goods and, as a result, continue to distort agricultural trade.

The process of tariffication created several tariffs at such stratospheric levels that it is difficult to conclude whether it was a good process that led to trade liberalization. Export

³³⁹ See *AoA* Art. 20.

³⁴⁰ GATT Art. XI 2(c) authorized import restrictions on any agricultural or fisheries product under specific circumstances.

³⁴¹ See *AoA* Preamble.

³⁴² Josling, Tim. "The Uruguay Round *Agreement on Agriculture: A forward-Looking Assessment*" *Paper prepared for a seminar at the Organisation for Economics Cooperation and Development (OECD), 1998*. (Paris: Institute for International Studies, 1998) [Josling, "Forward Looking Assessment"].

subsidies still exist, and a part of them was incorporated in a country's schedules. Hence, domestic subsidies programs from the main subsidizing countries were subject only to minor changes, and the Agreement on Modalities' negotiations have not come to a conclusion.

II.3.2.1 The Agreement on Modalities

The *AoA* divided the new obligations to trade in agriculture into three types of commitments. These complex sets of obligations were set up in the Agreement on Modalities (the Modalities)³⁴³ which established obligations that governments were supposed to comply with according to each set of commitments. However, it was never converted into a binding obligation. Instead, WTO Members converted the specific obligations to numerical scales that were displayed and classified under each country's schedules attached to the *AoA*.

The Agreement on Modalities established not only WTO Members' detailed schedules, but also a number of other general provisions. Therefore, in order to study the *AoA*, it is necessary to understand the general rules of the Modalities and the Agreement. The *AoA* itself is not a simple legal text. Almost every single provision has exceptions and additional implications for other agreements.

³⁴³ *AoA* Art. 20 gave the original mandate of the Agreement on Modalities. The Art. states that:

Recognizing that the long-term objective of substantial progressive reductions in support and protection resulting in fundamental reform is an ongoing process, Members agree that negotiations for continuing the process will be initiated one year before the end of the implementation period, taking into account: (a) the experience to that date from implementing the reduction commitments; (b) the effects of the reduction commitments on world trade in agriculture; (c) non-trade concerns, special and differential treatment to developing-country Members, and the objective to establish a fair and market-oriented agricultural trading system, and the other objectives and concerns mentioned in the preamble to this Agreement; and (d) what further commitments are necessary to achieve the above mentioned long-term objectives.

The Agreement can be found at GATT, *Agreement on Modalities for the Establishment of Specific Binding Commitments Under the Reform Programme*, GATT Doc. MTN.TNC/W/FA (1991), online: WTO <<http://docsonline.wto.org/gen. search/asp>> [*Modalities Agreement*].

An Agreement on Modalities is also being negotiated under the Doha Round. Regarding domestic support, the goal for the EU is to cut domestic support by 75%; the US and Japan, by 66%; and the rest of the Members, by 50%. With regard to market access, the goal is to cut tariffs according to a formula that was designed to make deeper cuts for higher tariffs. For developed countries, the cuts would rise from 50% for tariffs below 20%, to 66–73% for tariffs above 75%, whereas for developing countries, the cuts would raise from 50% for tariffs below 20% to 66–73% for tariffs above 75%. For developing countries, the cuts would be two thirds of the equivalent tier for developed countries. Lastly, the goal for export competition was to eliminate export subsidies by the end of 2013.³⁴⁴

The fact that the numerical goals are still being negotiated³⁴⁵ and were not agreed on by the Members demonstrates that the current legal framework on agriculture has not been able to successfully eliminate trade barriers. The *AoA* has more elaborate provisions, but the core of the negotiations (numbers on modalities) remains incomplete until the Doha Round is finished.

II.3.3 The *AoA*'s General Structure

The *WTO Agreement on Agriculture* encompasses three areas that compose the agricultural trade framework: market access, export subsidies, and domestic support.

“Market access” refers to procedures that regulate the level of access that imports have in the national market of the importing country. This includes regulation of tariffs, quotas and other import restraining measures. *AoA* Article 4.2 establishes the main obligation under the

³⁴⁴ WTO Committee on Agriculture, Special Section, *Revised Draft Modalities for Agriculture*, WTO Doc. TN/AoA/W/4/Rev.4 (6 December 2008), online: WTO http://www.wto.org/english/tratop_e/agric_e/chair_texts08_e.htm [*Modalities Agreement Revised*].

³⁴⁵ See Annex III about negotiations on Agricultural Subsidies.

Agreement: Members shall not maintain any measure that has been required to be converted into ordinary customs duties. The text refers to the “tariffication” process.

“Export subsidies,” as the name implies, are concerned with the extent to which Members can subsidize national products whose surpluses will be exported. *AoA* Articles 8, 9 and 10 regulate export subsidy commitments. Article 8 establishes that no Member shall provide export subsidies otherwise than in conformity with the *AoA* and in accordance with the commitments specified in each Member’s schedule.

The term “domestic support” refers to payments and other transfers of value given to domestic producers, regardless of the destination for their production. This category also includes indirect aids or subsidies, such as purchase commitments assumed by a government that have the effect of manipulating domestic prices at higher levels than those of the world market. *AoA* Arts. 6 and 7 regulate domestic agricultural support commitments. Art. 6 regulates the AMS procedures, and Art. 7 establishes that each Member must ensure that domestic support measures, not subject to reduction commitments, conform to the limits stipulated in the *AoA*. The provisions of the *AoA* on export and domestic subsidies will be analyzed next.

II.3.3.1 Export Subsidies

Part V of the *AoA* defines the regime for agricultural export subsidies.³⁴⁶ *AoA* Art. 8 states that “[e]ach Member undertakes not to provide export subsidies otherwise than in conformity with this Agreement and with the commitments as specified in that Member’s

³⁴⁶ Under the *Agreement on Agriculture*, export subsidies are defined in Art.1(e) as being contingent on export performance, including the export subsidies listed in detail in Article 9.

Schedule.” The *AoA* emphasizes that export subsidies have to be applied according to the limits established in the Agreement and in the schedules, which is corroborated by *AoA* Art. 3.3.³⁴⁷

In turn, Art. 9 defines *numerus clausus*, the export commitments subject to reduction commitments.³⁴⁸ The list includes subsidies not only directly given by governments but also by their agencies and indirect subsidies, such as the sale of non-commercial stocks under certain circumstances, especially when a charge on the public account is not involved. This list also includes subsidies on marketing, international transport and freight. Art. 9 also defines the methodology, the period of time and the reduction limits of export subsidization according to the rules and limits on the schedules.³⁴⁹

It should be noted that, from the second through the fifth years of the implementation period, export subsidies could be given in excess of the limits determined in the schedules if this

³⁴⁷ *AoA* Art. 3.3:

Subject to the provisions of paragraphs 2(b) and 4 of Article 9, a Member shall not provide export subsidies listed in paragraph 1 of Article 9 in respect of the agricultural products or groups of products specified in Section II of Part IV of its Schedule in excess of the budgetary outlay and quantity commitment levels specified therein and shall not provide such subsidies in respect of any agricultural product not specified in that Section of its Schedule.

³⁴⁸ Article 9.1 lists most of subsidies practices subjected to reduction commitments:

(a) the provision by governments or their agencies of direct subsidies including payments-in-kind, to a firm, to an industry, to producers of an agricultural product, to a cooperative or other association of such producers or to a marketing board, contingent on export performance; (b) the sale or disposal for export by governments or their agencies of non-commercial stocks of agricultural products at a price lower than the comparable price charged for the like product to buyers in the domestic market; (c) payments on the export of an agricultural product that are financed by virtue of governmental action, whether or not a charge on the public account is involved, including payments that are financed from the proceeds of a levy imposed on the agricultural product concerned or on an agricultural product from which the exported product is derived; the provision of subsidies to reduce the costs of marketing exports of agricultural products (other than widely available export promotion and advisory services) including handling, upgrading and other processing costs, and the costs of international transport and freight; (e) internal transport and freight charges on export shipments, provided or mandated by governments, on terms more favourable than the domestic shipments; (f) subsidies on agricultural products contingent on their incorporation in exported products.

³⁴⁹ *AoA* Art. 9:2(a):

... [T]he export subsidy commitment levels for each year of the implementation period, as specified in a Member's Schedule, represent with respect to the export subsidies listed in paragraph 1 of this Article: (i) in the case of budgetary outlay reduction commitments, the maximum level of expenditure for such subsidies that may be allocated ... in that year in respect of the agricultural product ... (ii) in the case of export quantity reduction commitments, the maximum quantity of an agricultural product, or group of products, in respect of which such export may be granted in that year.

excess was not above certain limits established in *AoA* Art. 9:2(b)³⁵⁰ and developing countries were not obliged to comply with certain reductions.³⁵¹

AoA Art. 10 establishes that no export subsidies authorized under *AoA* Art. 9 according to the limits on the schedules shall be applied in a manner that circumvents any export subsidy commitment. The *AoA* limitation on export subsidization is clear, even though there are exceptions of these limits regulated under Art. 9. Besides, there are possibilities to circumvent the numbers and percentages established in the schedules, as is going to be seen further below. Art. 10 also establishes some limits for international subsidies for food aid.³⁵²

It should be noted that the *AoA* does not contain a detailed definition of export subsidy. *AoA* Art. 1, which defined some terms in the Agreement, only states that “export subsidies” “refers to subsidies contingent upon export performance, including the export subsidies listed in Article 9 of this Agreement.”³⁵³ In *United States – Tax Treatment for Foreign Sales*

³⁵⁰ *AoA* Art. 9:2(b):

In any of the second through fifth years of the implementation period, a Member may provide export subsidies listed in paragraph 1 above in a given year in excess of the corresponding annual commitment levels in respect of the products or groups of products specified in Part IV of the Member’s Schedule, provided that: (i) the cumulative amounts of budgetary outlays for such subsidies ... does not exceed the cumulative amounts that would have resulted from full compliance with the relevant annual outlay commitment levels specified in the Member’s Schedule by more than 3 per cent of the base period level of such budgetary outlays; (ii) the cumulative quantities exported with the benefit of such export subsidies does not exceed the cumulative quantities that would have resulted from full compliance with the relevant annual quantity commitment levels specified in the Member’s Schedule by more than 1,75 per cent of the base period quantities; (iii) the total cumulative amounts of budgetary outlays ... over the entire implementation period are no greater than the totals that would have resulted from full compliance with the relevant annual commitment levels specified in the Member’s Schedule; and (iv) the Member’s budgetary outlays for export subsidies ... at the conclusion of the implementation period, are no greater than 64 per cent and 79 per cent of the 1986-1990 base period levels, respectively...

³⁵¹ *AoA* Art. 9:4 establishes that “[d]uring the implementation period, developing country Members shall not be required to undertake commitments in respect of the export subsidies ... provided that these are not applied in a manner that would circumvent reduction commitments.”

³⁵² *AoA* Art. 10:4: “Members donors of international food aid shall ensure: (a) that the provision of international food aid is not tied directly or indirectly to commercial exports of agricultural products to recipient countries; (b) that international food aid transactions, ... shall be carried out in accordance with the FAO “Principles of Surplus Disposal and Consultative Obligations” ... and (c) that such aid shall be provided to the extent possible in [according to] Article IV of the Food Aid Convention 1986”.

³⁵³ See *AoA* Art. 1(e).

Corporations [US – FSC],³⁵⁴ the panel stated that because the *AoA* does not have a definition of an export subsidy, it would apply the definition used by the *SCM Agreement* (transfer of economic resource from grantor to recipient). In the view of the panel, there would have to be a transfer of a resource, but also a benefit that was, in the case analyzed by the panel, a lower tax liability.³⁵⁵

The panel also considered the term “contingent upon export performance” in the same sense as applied in *SCM Agreement* Art. 3.1, which used the same expression. According to the panel, this expression meant that the subsidy was “dependent or conditional” on the exportation of the product or that it was provided before the exportation with an expectation that the product would be exported. The point here is that the panel condemned an export subsidy that was not listed in *AoA* Art. 9.1, which means that the *AoA* list was not exhaustive.³⁵⁶

In *Canada – Dairy*, the panel corroborated the view in *US – FSC*, that the definition of *AoA* Art. 1(e) covered more types of export subsidies than was specified in Art. 9.1. According to the panel, there was no inconsistency in the *AoA*’s rules, because the agricultural export subsidies that are not covered by the list in Art. 9.1 are covered by Art. 10.1, which states that “export subsidies not listed in paragraph 1 of Article 9 shall not be applied in a manner which results in ... circumvention of export subsidy commitments.”³⁵⁷ Therefore, export subsidies that are not able to meet all the practices listed in Art. 9.1 but are “subsidies contingent upon export performance” according to *AoA* Art. 1(e) are covered by Art. 10 and can be defined as export subsidies under the *AoA*.

³⁵⁴ Panel Report, *United States – Tax Treatment for “Foreign Sales Corporations”*, WT/DS108/R, at para. 138-142 adopted 20 March 2000, as modified by Appellate Body Report WT/DS108/AB/R, DSR 2000:IV, 1675 [*US – FSC*].

³⁵⁵ *Ibid.* at para 140.

³⁵⁶ *Ibid.* at 141-142.

³⁵⁷ *Canada – Dairy supra* note 223 at para. 7.125.

For this reason, the panel held that payments-in-kind and producer-financed schemes that might not fully comply with the elements of Art. 9.1 were included in the definition of agricultural export subsidies. Art. 9.1(a) states that direct subsidies from governments or their agencies, including payment-in-kind, are contingent upon export performance; the panel presumed that Art. 10.1 could cover an “indirect version of such subsidies.”³⁵⁸

In sum, the concept of export subsidy involves a governmental economic transfer that concedes a benefit to exports or those that were previously given, aiming at future exports, and the list that enumerates export subsidies in *AoA* Art. 9 is not exhaustive.

One of the subsidies listed in Art. 9(c) is “payments on the export of an agricultural product that are financed by virtue of governmental action, whether or not a charge in the public account is involved, including payments that are financed from the proceeds of a levy imposed on the agricultural product concerned.” The concept of “payments” was analyzed in *EC – Export Subsidies on Sugar*,³⁵⁹ which confirmed the decision in *Canada – Dairy*³⁶⁰ that determined that the ordinary meaning of the word “payment” “encompasses payments made in forms other than money.” In the first case, the high revenues resulting from sales of highly subsidized sugar A and B were used by producers to sell sugar C with prices significantly below the market prices, because of the cross-subsidization.³⁶¹ In the second dispute, the payments consisted of the provision of milk that would be exported at discounted prices.³⁶²

Both panels approached the concept of what the expression “financed by virtue of governmental action” meant. In *EC – Exports Subsidies on Sugar*, the panel confirmed that

³⁵⁸ *Ibid.*

³⁵⁹ Appellate Body Report, *European Communities – Export Subsidies on Sugar*, WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R adopted 19 May 2005, DSR 2005:XIII, 6365 [*EC – Exports Subsidies on Sugar*].

³⁶⁰ *Canada – Dairy* *supra* note 223

³⁶¹ *EC – Exports Subsidies on Sugar* *supra* note 359 at para. 259.

³⁶² *Canada – Dairy* *supra* note 223 at para. 7.90

“governmental action” meant “effective power to regulate, control or supervise individuals or otherwise restrain their conduct, through the exercise of lawful authority.”³⁶³ In *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products – Second Recourse to Article 21.5 of the DSU by New Zealand and the United States (Canada – Dairy Article 21.5 – New Zealand and US II)*, the concept established in *EC – Exports Subsidies on Sugar* was corroborated, and a link between governmental action and financing was stressed. The panel held that Canada had failed to establish that governmental action was not linked to the financing of payments analyzed by the case, and therefore, the panel considered that such payments had been “financed by virtue of governmental action.”³⁶⁴

In terms of challengeability, *AoA* Art. 13 establishes that export subsidies that fully comply with the limits established under *AoA* Part V (Arts. 9,10,11 and 12) can be countervailed only upon a determination of injury according to *GATT 1994* Art. V and the *SCM Agreement* Part V, and due restraint should be shown in initiating any countervailing duty investigation. The shield of the Peace Clause completely suspended challenges to export subsidies under *GATT 1994* XVI and under Art. 3, 5 and 6 of the *SCM Agreement*. During the *GATT 1947* years, as was seen, agricultural export subsidies were consistently condemned under *GATT 1947* Art. XVI when they gave “more than an equitable share of the world export trade” in the subsidized product to the subsidizing country.

At any rate, it can be stated that export subsidies were the pillar of the *AoA* that advanced the most during the Uruguay Round compared with domestic measures and market access. *AoA*

³⁶³ *EC – Export Subsidies on Sugar supra* note 359 at para. 235.

³⁶⁴ Panel Report, *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products – Second Recourse to Article 21.5 of the DSU by New Zealand and the United States*, WT/DS103/AB/RW2, WT/DS113/AB/RW2 at paras 5.91-5.93 adopted 17 January 2003, DSR 2003:I, 213 [*Canada – Dairy (Article 21.5 – New Zealand and US II)*].

Part V provides a list of export subsidies that should be in the Members' Schedules³⁶⁵ (Art. 8) and should be reduced (Art. 9), and some concepts of a possible definition of what constitutes an export subsidy were scrutinized.

The Schedules that determined the level of subsidization in a base period replaced the "equitable shares" defined under *GATT 1947* Article XVI:3 and the TRSC. For the first time, maximum levels of export subsidies were established for agricultural trade.³⁶⁶ The *AoA*'s provisions on export subsidies are clearly expressed in numeric commitments in the Schedules of the WTO Members that established reduction commitments.³⁶⁷ *AoA* Part V (Articles 8 to 11) and the Agreement on Modalities³⁶⁸ define and regulate export subsidies.

Basically, subsidy levels were limited and reduced both in terms of value and volume in the *AoA*. Members that did not subsidize exports during the base period were prohibited from doing so, except for certain agreed upon exceptions for developing country Members.³⁶⁹

³⁶⁵ The WTO explain the reduction commitments in the Schedule of each Member:

The reduction commitments are shown in the Schedules of WTO Members on a product-specific basis. For this purpose, the universe of agricultural products was initially divided into 23 products or product groups, such as wheat, coarse grains, sugar, beef, butter, cheese and oilseeds. Some Members took commitments on a more disaggregated level. The volume and budgetary outlay commitments for each product or group of products specified in a Member's Schedule are individually binding. The reduction commitments on "incorporated products" (last item in the Article 9 list) are expressed in terms of budgetary outlays only. The ceilings specified in the Schedules must be respected in each year of the implementation period although limited "over-shooting" in the second to fifth year of implementation is permitted ("downstream flexibility"). By the last year of the implementation period, Members must be within their final export subsidy ceilings. WTO, *Agriculture: Explanation, Export Competition/Subsidies*, online: WTO <http://www.wto.org/english/tratop_e/agric_e/ag_intro04_export_e.htm#reduction>

³⁶⁶ Josling, "Forward Looking Assessment" *supra* note 327 at 13.

³⁶⁷ 25 WTO Members can subsidize exports under the condition they reduce these subsidies. The Members that did not have reduction commitments cannot subsidize agricultural exports at all. The 25 countries follow with the number of the products they have commitments: Australia (5), Brazil (16), Bulgaria (44), Canada (11), Colombia (18), Cyprus (9), Czech Rep (16), EU (20) Hungary (16), Iceland (2), Indonesia (1), Israel (6), Mexico (5), New Zealand (1), Norway (11), Panama (1), Poland (17), Romania (13), Slovak Republic (17), South Africa (62), Switzerland-, Liechtenstein (5), Turkey (44), United States (13), Uruguay (3) and Venezuela (72). WTO, Committee in Agriculture, Special Section, Export Subsidies, Background Paper by the Secretariat, WTO Doc. TN/*AoA*/S/8 (9 April 2002), online: WTO <http://www.wto.org/english/tratop_e/agric_e/negs_bkgnd06_export_e.htm>

³⁶⁸ Even though the Modalities Agreement has no legal effect, it served as parameter to calculate indicators and commitments for tariff reductions.

³⁶⁹ The main reduction commitments affect OECD countries, particularly the European Union, which is the major user, accounting for 90 percent of actual export subsidies notified to the WTO for the 1995-98 period. Organization

The reductions adopted at that time were 36% for budget outlays and 21% for the quantities of export aid, both being measured from outlays and quantities in the implementation period from 1986-1990.³⁷⁰ During the negotiations, export subsidy commitments were converted into specific numeric commitments for each Member and recorded in a Schedule to the Agreement. Similar to the market access commitments, the practical legal obligations defining the basic commitments on export subsidies were the transformed numeric commitments in the schedules.

However, the success of the regulation of export competition in the Uruguay Round was limited. The share of world exports covered by export subsidies was significant for major agricultural products, particularly grains, livestock products and sugar. The EC subsidized “more than 95 percent of its exports of wheat and butter ... more than 90 percent of cheese exports, 40 percent of sugar exports and more than 30 percent of milk powder for the same destination.” The US subsidized export in “butter (94 percent), wheat (55 percent), non-fat dry milk (40 percent) and cheese (23 percent),”³⁷¹ to name a few products.

Besides, there were several cases challenging export subsidies after the Uruguay Round. In *US – Upland Cotton*, the Appellate Body held that the panel did not err in finding that “the GSM 102 export credit guarantee program constituted an export subsidy ... under the terms of item (j) of the illustrative list ... and Agriculture Agreement Article 10.1.”³⁷² In *US – Tax Treatment for Foreign Sales Corporations. Second Recourse to Article 21.5 of the DSU by the*

for Economic Co-operation and Development, OECD Highlights from the 16th Edition, “Agricultural Policies in OECD Countries: Monitoring and Evaluation” (2004).

³⁷⁰ *Modalities Agreement supra* note 344 at para. 11.

³⁷¹ Merlinda Ingco, “Agricultural Liberalization in the Uruguay Round: One Step Forward, One Step Back?” *Policy Research Working Paper 1500 prepared for a World Bank Conference on “The Uruguay and the Developing Countries, 1995* (Washington D.C.: WB IED ITD, 1995) at 8 [Ingco “Agricultural Liberalization”].

³⁷² *US – Upland Cotton supra* note 8 at paras. 255-323.

*European Communities [US – FSC (Article 21.5 EC II)]*³⁷³ the Appellate Body found that the US continued to fail to fully implement the operative DSB recommendation to withdraw the prohibited export subsidies, which were inconsistent with *AoA* Arts. 10.1, 8 and 3.3.

In *EC – Export Subsidies on Sugar*, the Appellate Body upheld the panel’s finding that the European Communities acted inconsistently with Agriculture Agreement Arts. 3.3 and 8 by “providing export subsidies on sugar in excess of its commitment levels specified in its schedule.”³⁷⁴ In *Canada – Dairy Article 21.5 – New Zealand and US II*, the Appellate Body upheld the panel’s finding that, by providing export subsidies, as defined in Article 9.1(c), in excess of the quantity reduction commitment levels specified in its schedule for exports of cheese and other milk/dairy products, Canada had acted inconsistently with Arts. 3.3 and 8.³⁷⁵

These cases demonstrate that export subsidization is not only a practice that was not eliminated after the Uruguay Round but also that it is being done above the limits of the schedules and, for this reason, still represents a substantial distortion in world agricultural trade. There is also criticism related to the level of export subsidization after the Uruguay Round. It has been stated that this kind of subsidy was reduced for several goods but that there are some specific products whose subsidies still represent a substantial distortion in world agricultural trade.³⁷⁶

³⁷³ Appellate Body Report, *US – Tax Treatment for Foreign Sales Corporations. Second Recourse to Article 21.5 of the DSU by the European Communities* (2006), WTO Doc WT/DS108/AB/R W2 at paras 70-96 adopted 14 March 2006, DSR 2006:XI, 4721 [*US – FSC (Article 21.5 – EC II)*].

³⁷⁴ *EC – Exports Subsidies on Sugar* *supra* note 359 at paras 227-290.

³⁷⁵ *Canada – Dairy (Article 21.5 – New Zealand and US II)* *supra* note 364 at paras 155 – 156.

³⁷⁶ “the allowable volume of export subsidies for major commodities at the end of the implementation period will remain substantial, with the largest amounts remaining in wheat (over 40 million tons), coarse grains (nearly 20 million tons) beef and ... vegetable oils (about 1 million tons). Hathaway & Ingco, *Agricultural Liberalization* *supra* note 318 at 10.

II.3.3.2 Domestic Support

The analysis in the previous section showed that some provisions of the *AoA* and some WTO cases helped to elucidate the concept of export subsidies; however, there is neither a clear definition of “agricultural domestic support commitments” in *AoA* Art. 6 and 7, which regulate this sort of agricultural subsidy nor any WTO case that helps to elucidate this concept. In general terms, “agricultural domestic support commitments” refer to transfers of any value given to domestic producers that, differently from export subsidies, can be provided for products with no regard for their destination.

Hudec explains that agricultural domestic support commitments do not exclude other measures intended to artificially manipulate domestic market prices, such as administered prices support or government purchase commitments.³⁷⁷ And they include “both product-specific subsidies and transfers of value” that might not be related to any product. Similar to the concept of agricultural export subsidies, domestic support commitments involve not only the transfer of money, but also other indirect forms of artificial support, such as governmental purchases.

The *GATT 1994* did not have any specific provisions for the regulation of domestic subsidies, especially for agriculture. The limitation for agricultural subsidization during the *GATT 1947* years was related to export subsidies under Art. XVI and nullification or impairment under Art. XXIII 1(b).

³⁷⁷ Robert E. Hudec, “Does the *Agreement on Agriculture* work? Agricultural Disputes after the Uruguay Round” *Working Paper # 98-2 International Agricultural Trade Research Consortium # 98-2, 1998* (St. Paul: University of Minnesota, 1998) at 27 [Hudec, *Does the AoA work?*].

The *AoA* requires governments to identify and quantify domestic support measures for any agricultural product receiving market price support, non-exempt direct payments or any other subsidy not exempt from the reduction commitment. The total amount of such support measures is called the Aggregate Measurement of Support (AMS).³⁷⁸ The Agreement also requires Members to not only bind AMS levels at their 1986-88 levels,³⁷⁹ but also to reduce the AMS levels 20% during the implementation period, which was six years for developed countries or 13.3 percent over 10 years for developing country Members.³⁸⁰ The effective legal obligations for domestic support are the numerical commitments recorded in the schedules attached to the *AoA* that were converted from the rules in the Modalities. In any year of the implementation period, the total AMS value of non-exempt measures must not exceed the scheduled total AMS limit for that year.³⁸¹

According to the provisions of *AoA* Art. 6, the AMS has to be calculated on “product-specific basis” if the product receives market price support, non-exempt direct payment or any subsidy that is not exempt from reduction commitments established in the *AoA*. Subsidies have to include both budgetary outlays and revenue foregone. National and sub-national subsidies

³⁷⁸ *AoA* Article. 1 (a) establishes:

Article 1. *Definition of Terms*. In this Agreement, unless the context otherwise requires: (a) “Aggregate Measurement of Support” and “AMS” mean the annual level of support, expressed in monetary terms, provided for an agricultural product in favour of the producers of the basic agricultural product or non-product-specific support provided in favour of agricultural producers in general, other than support provided under programmes that qualify as exempt from reduction under Annex 2 to this Agreement, which is: (i) with respect to support provided during the base period, specified in the relevant tables of supporting material incorporated by reference in Part IV of a Member’s Schedule; and (ii) with respect to support provided during any year of the implementation period and thereafter, calculated in accordance with the provisions of Annex 3 of this Agreement and taking into account the constituent data and methodology used in the tables of supporting material incorporated by reference in Part IV of the Member’s Schedule.

³⁷⁹ *AoA* Annex 3:9-11.

³⁸⁰ The results of the negotiations in which participants have made commitments to eliminate or reduce tariff rates and non-tariff measures applicable to agriculture are recorded in national schedules of concessions annexed to the Uruguay Round Protocol that forms an integral part of the Final Act. WTO, “Legal Texts: the WTO Agreements: A Summary of the Final Act of the Uruguay Round”, online: WTO <http://www.wto.org/english/docs_e/legal_e/ursum_e.htm>

³⁸¹ *AoA* Article 6.3

have to be considered in the calculations, and agricultural levies or fees paid by producers have to be deducted. The AMS has to be calculated separately for each basic agricultural product in total monetary value terms.³⁸²

For the purpose of current total AMS calculations, price support is generally measured by multiplying the gap between the applied administered price and a specified fixed external reference price (world market price) by the quantity of production eligible to receive the administered price. Calculation details are specified in Annexes 3 and 4 of the *Agreement on Agriculture* and are incorporated into Members' schedules by way of references to supporting material.³⁸³

Several countries have a variety of domestic support programs that are not properly converted into numeric commitments. As was seen, several rules have to be observed for a proper conversion, and the process is complex. This process of conversion has subjective elements, because it depends on the concept of domestic programs for the Members doing the converting and on how they would measure them. Therefore, it can be said that the AMS does not represent a significant restraint on trade-distorting practices.

Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef [*Korea – Various Measures on Beef*]³⁸⁴ illustrates how tricky and uncertain can be the process of quantifying domestic support measures in the AMS. Australia and the US complained that Korea's domestic support for beef in 1997 and 1998 had exceeded the reduction commitments contained in the schedule of the country. The panel held that Korea's support measures for beef were inconsistent with *AoA* Articles 3, 6 and 7. Korea appealed, and the Appellate Body reversed

³⁸² *AoA* Annex 3:1-7.

³⁸³ *AoA* Annex 3:8.

³⁸⁴ Appellate Body Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, WTO Doc. WT/DS161/AB/R, adopted 10 January 2001, DSR 2001:I, 5 [*Korea – Various Measures on Beef*].

the panel's decision that Korea had exceeded its AMS commitment levels in violation of the *AoA*.

The Appellate Body held that Korea had miscalculated the current AMS for beef, but the panel relied on figures presented by New Zealand that were not correct either. Based on New Zealand's figures, the panel had concluded that Korea's AMS for beef had exceeded the *de minimis* levels established in *AoA* Article 6.4. However, these figures were not calculated in accordance with *AoA* Annex 3. Therefore, the Appellate Body reversed the panel's conclusion that Korea's 1997 and 1998 AMS for beef had exceeded the *de minimis* levels. However, it found it was unable to complete this legal analysis because of "insufficient factual findings made by the panel."³⁸⁵

This case exemplifies the subjective elements of the AMS calculation, even though it did not represent a very significant restraint on trade-distorting practices in domestic support measures. The complainant alleged that the AMS calculations of the respondent were wrong. The panel agreed with the complainant, but the AB reversed the decision, stating that the calculations were wrong.

The *AoA* categorizes domestic support policies in "boxes" according to their potential to distort production and trade. It also imposes some reduction commitments on the most trade-distortive category: the "amber box" policies. Some countries, however, anticipated the implementation of the *AoA* Agreement and changed their agricultural policies before the conclusion of the Uruguay Round. The EU, the United States and Canada, for example, replaced market price supports that caused excess of production with more direct income payments and

³⁸⁵ *Ibid.* at paras 123 – 127, 186 (c) and (d).

other less distorting measures. This, however, does not necessarily mean that those measures do not affect production or trade.³⁸⁶

According to the definition in session II.3.1.2, AoA Art. 6 defines amber box subsidies as the domestic measures that support price or are directly related to production quantities. For this reason, they are likely to distort trade and are subject to reduction commitments according to each WTO Member's schedule and to *de minimis* levels established by AoA Art. 6.4, under which supports are allowed. The levels are 5% of product-specific domestic support and non-product-specific domestic support and 10% for developing countries.³⁸⁷

Many exempt support measures, such as certain types of domestic subsidies, while certainly less trade-distorting than non-exempt measures, still have production and trade effects. They reduce planting risks and foster production. The amount of the payment, as well as the detailed design and duration of a support program, is a critical factor for determining the impact of policies on production and trade.

Green box programs are classified as the support measures that have the least distortive effects on production and trade. In fact, the fundamental criterion for green box exemptions is that they have “no, or most minimal” effects on trade and also “shall not have the effect of providing price support to producers”.³⁸⁸ They might include direct support for farmers but are

³⁸⁶ Not all domestic subsidies had to comply with reduction commitments. On the contrary, in the OECD, almost 60 percent of domestic agricultural support in OECD countries is excluded from the domestic reduction commitments. During the implementation period, the composition of some OECD countries domestic support has changed. Reduction of total current AMS was simultaneously accompanied by an increase in exempt support, particularly in green box support. The largest increases in green box expenditures were recorded in the European Union, Japan, and the United States. Over the implementation period, green box support was higher than AMS support. See Tangermann “Has the UR worked well?” *supra* note 309.

³⁸⁷ AoA Art. 6.4.

³⁸⁸ AoA Annex 2:1:

Domestic support measures for which exemption from the reduction commitments is claimed shall meet fundamental requirement that they have no, or at most minimal, trade-distorting effects or effects on production. Accordingly, all measures for which exemption is claimed shall conform to the following basic criteria: (a) the support in question shall be provided through a publicly-funded government programme

not supposed to be given to particular products and must be decoupled from production levels or prices. They are divided into categories, the first one comprising general services that include research, pest and disease control, training services, advisory services, inspection services, marketing and promotion services and infrastructural services.³⁸⁹

The other categories include food aid³⁹⁰; direct and indirect (revenue foregone) payments and decoupled income support under the condition that it does not involve a transfer from consumers and does not constitute price support to producers;³⁹¹ government support for safety net programs and for relief from natural disasters;³⁹² assistance for producer and resource retirement programs;³⁹³ structural adjustment assistance provided through investment aids;³⁹⁴ payments for environmental programs;³⁹⁵ and payments for regional assistance programs.³⁹⁶

It should be noted that green box subsidies are an extensive list of subsidies that hypothetically do not distort trade. *AoA* Annex II enumerates 13 possible green subsidies, and each has a list of requirements with a certain level of complexity. However, the possibility of allocation of distortive subsidies to sit under under the “green cloth” remains. It should also be stated that the use of direct payments from government to producers must not interfere with the volume and type of agricultural production, which means that the green subsidy has to be decoupled from agricultural production. However, in practical terms, it is difficult to imagine a

(including government revenue foregone) not involving from consumers; and (b) the support in question shall not have the effect of providing price support to producers; ...

³⁸⁹ *AoA* Annex 2:2.

³⁹⁰ Public stockholding for food security purposes, domestic food aid. *AoA* Annex 2:3-4.

³⁹¹ Direct payment to producers and decoupled income support. *AoA* Annex 2:5-6.

³⁹² The eligibility for support for safety net programmes shall be terminated by an income loss taking into account only income derived from agriculture, which exceeds 30 per cent of average gross income and for relief of natural disasters, a formal recognition of national authorities that a disaster has occurred. *AoA* Annex2:7-8.

³⁹³ Conditions established in *AoA* Annex 2:9-10.

³⁹⁴ It makes possible reprivatization of agricultural lands possible if the payment is limited to the amount required to compensate for the structural disadvantage. *AoA* Annex2:11.

³⁹⁵ There must be a clear governmental plan of conservation and the amount of payment has to be limited to the extra costs or loss of income possibly involved in complying with the plan. *AoA* Annex 2:12.

³⁹⁶ The eligibility of this subsidy must be limited to producers in disadvantaged regions and the amount shall not be linked to the type or volume of production, among other requirements established on *AoA* Annex II:13.

payment given to a farmer that will not interfere in the production of his crop. The term “decoupled” has been constantly discussed in the WTO.³⁹⁷

Changes in the mix of domestic support policies towards green box measures are supposed to lead to a reduction in production and trade distortions. However, whether all green box payments or measures have no, or at most minimal, trade and production effects is not clear, because the *AoA*'s eligibility criteria for green box measures cannot guarantee no or minimal trade distortions.³⁹⁸ The *AoA*'s provisions establishing criteria for green box policies focus on the way in which policies are implemented rather than on the limit or the amount of the subsidy. The maximum limits agreed upon for domestic support are based on the level of "distorting" support provided by each country during the 1986-88 base period. The problem is that some countries that widely used production and price support policies did not report their support levels.³⁹⁹

Besides the green box measures, *AoA* Art. 6 exempts from reduction commitments measures of assistance to encourage rural development in developing countries and to help them to combat the growing of illicit narcotic crops.⁴⁰⁰ As was seen above, product-specific and non-product-specific domestic subsidies are limited by *de minimis* levels.⁴⁰¹

³⁹⁷ See *US – Upland Cotton supra* note 14.

³⁹⁸ Several blue box and green box measures in WTO classification are included in the OECD PSE calculation and some of them as payments based on outputs. OECD, Economics Department, *Agricultural Policy Reform: The Need for Further Progress* OECD Economic Outlook 70, Agriculture Policies in OECD countries: Monitoring and Evaluation, (Paris: OECD, 2000).

³⁹⁹ According to the OECD data, after the Uruguay Round only 30 WTO Members had total AMS reduction commitments. Domestic support is highly concentrated in a few OECD countries with the European Union, Japan, and the United States accounting for 90 percent of total domestic support (that is, AMS blue box, green box, *de minimis*, and special and differential treatment). Merlinda D. Ingco & L. Alan Winters, eds., *Agriculture and the New Trade Agenda: Creating a Global Trading Environment for Development* (New York: Cambridge University Press, 2004) at 57.

⁴⁰⁰ *AoA* Art. 6:2 establishes:

In accordance with the Mid-Term Review Agreement that government measures of assistance, whether direct or indirect, to encourage agricultural and rural development are an integral part of the development programmes of developing countries, investment subsidies which are generally available to agriculture in developing country Members and agricultural input subsidies generally available to low-income or

The blue box subsidies are direct payments under production-limiting programs considered trade distorting but at a lower level if compared with the amber box subsidies related to price support measures. However, these payments have to be coupled with production. As previously stated, payments may be directly dependent on production so long as the payment is based on a determined area and yields, the volume does not exceed 85% of production in the base period or a livestock payment is based on a fixed number of head.⁴⁰²

The *AoA* establishes limits for the challengeability of subsidies according to qualitative definitions and has established some exceptions to challenges: *de minimis* (*AoA* Art. 6.4) and developing countries under *AoA* Art. 6.2. As was seen, there is a significant number of subsidies in the green box that were not challengeable during the peace period, but were potentially distortive to trade. This was one of the flaws of the domestic support's legal framework established in the Uruguay Round. Green box subsidies allowed many subsidies to continue to be used at the same level as prior to the Uruguay Round. Furthermore, the EU compensation payments and the US deficiency payments (blue box measures) were exempted from the reduction commitments, even though they could not be considered neutral.⁴⁰³

In regards to the challengeability of domestic support measures, Article 13 completely exempted green box domestic support measures from actions based on nullification and impairment (*GATT 1994* Article. XXIII 1(b)), countervailing duties, *SCM Agreement* measures

resource-poor producers in developing country Members shall be exempt from domestic support reduction commitments that would otherwise be applicable to Members to encourage diversification from growing illicit narcotic crops. Domestic support meeting the criteria of this paragraph shall not be required to be included in a Member's calculation of its Current Total AMS.

⁴⁰¹ *AoA* Article 6.4

⁴⁰² *AoA* Article. 6:5 (a) ii

⁴⁰³ One of the EU requirements for the completion of the Uruguay Round on agriculture was that the blue box subsidies were waived from reduction commitments (in the same way green box are exempted). The blue box measures were intend to shield compensatory European compensatory payments and American direct payments make contingent on production limitation requirements. Melaku Geboye Desta, *The Law of International Trade in Agricultural Products: From GATT to the WTO Agreement on Agriculture* (London: Kluwer Law International. London, 2002) at 393 [Desta, *Trade in Agriculture*].

and *GATT 1994* Art. XVI, because they were purportedly not trade distorting. Some scholars say these exemptions were created to encourage governments to convert support measures to this non-distortive form, which did not happen. On the contrary, some Members started to classify distortive domestic support measures as green so that they could not be actionable.

Blue box domestic support measures were exempted from the imposition of countervailing duties, unless a determination of injury was made. They were exempted from actions based on *GATT 1994* Art. XVI, *SCM Agreement* Arts. 5 and 6, and *GATT 1994* Art. II and XXIII 1(b) if these measures were not given in excess of those of the 1992 marketing year. It is true that there is no extremely significant exemption from countervailing duties for trade-distortive measures, because in this case injury can be proved. But *AoA* Art. 13 was a significant restraint for challengeability during the Peace Clause years.

The *AoA* created a framework for domestic support commitments that the *GATT 1994* did not have. For this reason, the domestic support discipline introduced by the *AoA* can be considered a landmark in the history of international trade in agriculture. However, the mere existence of this framework of the *Agreement on Agriculture* is not proof that the *AoA*'s domestic support commitments are more efficient than *GATT 1994* provisions for domestic subsidies.

There are still several exceptions for production-distorting domestic support. The so-called green and blue box measures are free of any reduction commitment, even though they might distort trade. In fact, very few subsidies would not have any effect on trade.⁴⁰⁴

Even the amber box measures are not subject to significant restraint obligations. Firstly, the American deficiency payments and European compensatory payments (blue box measures)

⁴⁰⁴ Tangermann, "Agriculture and Developed Countries" *supra* note 275 at 207. See also Bernard Hoekman & Kym Anderson, "Developing Country Agriculture and the New Trade Agenda" *Policy Research Working Paper 2125, 1999* (Washington D.C.: The World Bank, Development Research Group, 1999) at 12.

were not included in the amber box, even though they cause a high level of distortion. Secondly, the only restraint for amber box measures would be possible challengeability that was partially shielded by the Peace Clause during the “peace period.” Therefore, for nine years (from January 1, 1995, when the Uruguay Agreements were implemented, until December 31, 2003, when the Peace Clause ended), even the amber box support measures were almost⁴⁰⁵ free from any challengeability.

The incorrect application of the exception for non-distortive trade measures, application of *de minimis* for support that did not exceed 5% of the total value of that product’s production and distortive blue box subsidies not included in the amber box illustrate some weaknesses of the system. Moreover, the selection of the base period for the AMS calculation had a historic peak for many commodities and countries.⁴⁰⁶ Therefore, in practical terms, the provisions for domestic support measures provided during the Uruguay Round were not successful in hindering trade distortions in agriculture.

The ongoing agricultural negotiations in the Doha Round still have to redefine the future path of agricultural trade liberalization. Moreover, the *AoA* will not make significant progress towards market-determined production levels if the Doha Round ends in a deadlock. Support-reducing commitments still have to be negotiated.⁴⁰⁷

⁴⁰⁵ The only possibility for challengeability against free domestic subsidization was under the *SCM Agreement* or GATT 1994 in cases where the subsidy exceeded that for the 1992 marketing year.

⁴⁰⁶ OECD, *The Uruguay Agreement on Agriculture: An evaluation of its Implementation in OECD Countries* (Paris: OECD, 1995) at 44.

⁴⁰⁷ See Annex III

II.4 Challenges to Agricultural Subsidies During the Peace Period

During the period shielded by the Peace Clause, from January 1, 1995, to December 31, 2003, there were just a few challenges to agricultural subsidization. Only eight of 53 groups⁴⁰⁸ of disputes challenged agricultural subsidies during the peace period.⁴⁰⁹ There were two countervailing duty cases (one consultation and one panel), two consultations and four cases that took a long time to be resolved.⁴¹⁰ The significantly low number of cases and the length of time to resolve them is an indication of how difficult it was to challenge agricultural subsidies during the period of the Peace Clause.

The first consultation was *Hungary – Export Subsidies in Respect of Agricultural Products [Hungary – Agricultural Products]*.⁴¹¹ In 1996, Australia and other complainants required consultations, alleging possible violation by Hungary of AoA limits for export agricultural subsidization. On July 30, 1997, the DSB was notified that the parties had reached a mutually agreed to solution, and for this reason, Hungary would seek a waiver of certain WTO obligations.⁴¹²

⁴⁰⁸ For the purposes of this study, the same group of cases concern disputes that challenge the same measures and have the same parties.

⁴⁰⁹ WTO, *Disputes by Agreement*, online: WTO <http://www.wto.org/english/tratop_e/dispu_e/dispu_Agreements_index_e.htm?id=A1#selected_Agreement>.

⁴¹⁰ The *US – FSC* case took almost eight years. The *Canada – Dairy* case took six years. The *EC – Exports Subsidies on Sugar* took four years until a final Agreement between the parties was settled. The AB decision of *US – Upland Cotton* has not been applied yet and the dispute lasts more than 8 years. It is acknowledged, however, that the cases are highly complex and the goals the parties are seeking through the case need a certain amount of time to be achieved. According to the WTO “[b]y January 2008, only about 136 of the nearly 369 cases had reached the full panel process. Most of the rest have either been notified as settled “out of court” or remain in a prolonged consultation phase — some since 1995.” WTO, *A Unique Contribution – Understanding the WTO, settling disputes*, online: WTO <http://www.wto.org/english/thewto_e/whatis_e/tif_e/disp1_e.htm>

⁴¹¹ Request for the Establishment of a Panel by the United States, *Hungary – Export Subsidies in respect of Agricultural Products* (1997) WTO Doc. WT/DS35/7, circulated 10 January 1997 (97-0082) [*Hungary – Agricultural Products*].

⁴¹² WTO, *Hungary – Export Subsidies in respect of Agricultural Products*, online: WTO < WTO, *Disputes by Agreement*, online: WTO <http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds35_e.htm>.

The second consultation was *European Communities – Measures Affecting the Exportation of Processed Cheese [EC – Exportation of Cheese]*.⁴¹³ In 1997, the US requested consultations with the EC regarding export subsidies for processed cheese that were at higher levels than was established in the schedules. The US alleged that these measures violated *AoA* Arts. 8, 9, 10 and 11 and *SCM Agreement* Art. 3. A panel was not established, and the case did not go further.

The first group of cases challenging agricultural subsidies during the peace years was *Canada – Dairy*.⁴¹⁴ The US and New Zealand challenged Canadian export subsidies for dairy products under, among other provisions, *SCM Agreement* Art. 3. A single panel was established to analyze both disputes. The panel decided that agricultural subsidies could only be subject to *SCM Agreement* Art. 3 if they exceeded the levels permitted under the *AoA*. For this reason, panelists decided to first analyze the measures under the relevant provisions of the *AoA* and then, if necessary, under *SCM Agreement* Art. 3.⁴¹⁵ The Canadian subsidies were declared illegal under *AoA* Art. 3.3 and 8 and *GATT 1994* Art. II:1(b) by the panel and by the AB.

In 2001, New Zealand requested the implementation of the Art. 21.5 panel's⁴¹⁶ recommendations so as to remove the implementation's obstacles. The Appellate Body reversed some decisions of the panel that condemned original and new dairy subsidies under *AoA* Art. 9.1(c) and was unable to conclude about the challenge under *SCM Agreement* 3.1. In the same year, the US and New Zealand filed a second recourse this time for the establishment of a panel pursuant to DSU Art. 21.5. Canada requested arbitration under DSU Art. 22.6, but the parties

⁴¹³ Request for Consultations by the United States, *European Communities – Measures Affecting the Exportation of Processed Cheese* (1997) WTO Doc. WT/DS104/1, G/AoA/GEN/13, G/SCM Agreement/D16/1, circulated 18 October 1997 (97-4384) [*EC – Exportation of Cheese*].

⁴¹⁴ *Canada – Dairy* *supra* note 223.

⁴¹⁵ *Ibid.* at paras. 7.18-31.

⁴¹⁶ DSU Art. 21.5 establishes if there is disagreement about measures taken to comply with the decision, there must be another 90 days panel to decide the matter. It is a compliance panel.

agreed that it would be suspended until the final decision of the second recourse, which also condemned dairy subsidies under the same *AoA* provisions. This decision was adopted by the DSB in January 2003.

In May 2003, Canada, the US and New Zealand informed the DSB that they had reached an agreement under DSU Art. 3.6⁴¹⁷ in both dairy disputes. The dairy cases started in 1997 and were settled in 2003 after two main panels, two recourses to DSU 21.5 and one recourse to DSU 22.6 arbitration. On some occasions the AB reversed determinations of illegality, and several times the parties asked that the procedures be suspended for negotiations. Eventually, the cases were settled, after almost six years of litigation. During this period, agricultural subsidies declared incompatible with the *AoA* and *SCM Agreement* continued to be given.

The second group of cases was *US – FSC*. In 1997, the EC requested consultations with the US about Sections 921 and 927 of the US Internal Revenue Code and related measures that established special tax treatment for foreign sales corporations [FSC]. According to the EC, these provisions violated *SCM Agreement* Art. 3.1 (a) and (b) and *AoA* Arts. 3 and 8. The reason was that they were considered export subsidies under the *AoA*, were available in quantities that exceeded the reduction commitment levels and were also given to some unscheduled products, which was also a violation of *AoA* Art. 3.3.⁴¹⁸ In 2000, the AB upheld the condemnation under *SCM Agreement* Art. 3.1 but reversed the panel's decision that the subsidies were agricultural according to *AoA* Art. 9.1(d), and therefore, it reversed the *AoA* Art. 3.3 violation decision.⁴¹⁹

In the same year, the EC made a request to the DSB that the implementation of DSU Art. 21.5 panel and procedures of DSU Art. 22.6 be suspended until a decision could be reached. In

⁴¹⁷ DSU Art. 3.6 establishes that “mutually agreed solutions ... shall be notified to the DSB ... where any Member may raise any point relating thereto.”

⁴¹⁸ *US – FSC supra* note 354 at para. 160.

⁴¹⁹ Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations"*, WT/DS108/AB/R, at paras. 59-61 and 122 adopted 20 March 2000, DSR 2000:III, 1619 [*US – FSC*].

2001, the panel held that the FSC Repeal and Extraterritorial Income Exclusion Act of 2000, which had been enacted to replace the condemned FSC legislation, was also inconsistent with *SCM Agreement* Art. 3 and *AoA* Art. 10.1 and 8. This decision was upheld by the AB in 2002.

In 2005, the EC requested of the DSB the establishment of another DSU Art. 21.5 panel. It was established, and the amended FSC American legislation was considered inconsistent with the *AoA* and *SCM Agreement*. This decision was upheld by the AB in 2006 with the statement that the US “continued to fail to implement fully the operative DSB recommendations and rulings to withdraw the prohibited subsidies and to bring its measures into conformity with its obligations under the relevant Agreements.”⁴²⁰

After almost eight years of dispute, the panel decided that the US – amended FSC legislation was still violating WTO agreements, but on May 17, 2006, the parties notified the DSB that they had reached an agreement.

The third group of cases was *EC – Export Subsidies on Sugar* complained by Australia (DS 265)⁴²¹ and by Brazil (DS 266).⁴²² In September 2002, both countries asked for consultations with the EC concerning the Community’s export subsidies legislation for sugar, especially regarding Regulation (EC) 1260/2001. In 2003, Thailand requested consultations with the EC about the same measures.⁴²³ Several countries joined the consultations.⁴²⁴

⁴²⁰ *US – FSC (Article 21.5 – EC II supra* note 373 at para. 96.

⁴²¹ Panel Report, *European Community – Export Subsidies on Sugar* (2005), WTO Doc. WT/DS 265/R adopted 19 May 2005, as modified by Appellate Body Report WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, DSR 2005:XIII, 6499 [*EC – Export Subsidies on Sugar (Australia)*].

⁴²² Panel Report, *European Community – Export Subsidies on Sugar* (2005), WTO Doc. WT/DS 266/R adopted 19 May 2005, as modified by Appellate Body Report WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, DSR 2005:XIV, 6793 [*EC – Export Subsidies on Sugar (Brazil)*].

⁴²³ Panel Report, *European Communities – Export Subsidies on Sugar, Complaint by Thailand* (2005), WTO Doc. WT/DS283/R, adopted 19 May 2005, as modified by Appellate Body Report WT/DS265/AB/R, WT/DS266/AB/R, WT/DS283/AB/R, DSR 2005:XIV, 7071 [*EC – Export Subsidies on Sugar (Thailand)*].

⁴²⁴ The dispute involved around 20 Members. In the dispute WT/DS265, Barbados, Belize, Brazil, Canada, Colombia, Congo, Côte d’Ivoire, Fiji, Guyana, India, Jamaica, Kenya, Madagascar, Malawi, Mauritius, St. Kitts and Nevis, Swaziland and Zimbabwe requested to join the consultations. On 24 October 2002, the EC informed the DSB that it had accepted the requests of Barbados, Belize, Brazil, Canada, Colombia, Congo, Côte d’Ivoire, Fiji, Guyana,

The complainants alleged that the EC was exporting subsidized sugar in excess of its commitments in the schedules of concessions, which violated *AoA* Arts. 3 and 8. It was also alleged that Sugar C was receiving export subsidies in excess of its commitment levels, which violated *AoA* Art. 9.1(c). The allegations that these subsidies violated *AoA* Art. 10.1 and *SCM Agreement* Art. 3.1(a) were not analyzed by the panel for reasons of judicial economy.

In 2004, the panel circulated separated but equal reports on the complaints of Brazil (WT/DS 265), Australia (WT/DS 266) and Thailand (WT/DS283), determining that the EC's exports of sugar had exceeded annual commitment levels since 1995. These subsidies violated *AoA* Art. 9.1(c). The EC had not demonstrated that exports of a specific type of sugar in excess of its annual commitment were not subsidized. For this reason, the EC had violated *AoA* Arts. 3.3 and 8. The EC appealed, and the AB upheld the panel's decision on inconsistencies in the EC's sugar subsidies and decided that the panel erred in not ruling on the complainants' claims under the *SCM Agreement*.

In the appeal, the EC alleged that the panel had erred in condemning its subsidies under *AGA* Art. 9.1(c) and in determining that these subsidies had caused nullification or impairment of benefits for the complainants. The complainants also appealed the decision of the panel to exercise judicial economy regarding *SCM Agreement* Art. 3 claims.

The EC alleged that, in footnote 1 in Section II, Part IV of its schedule, there was a statement that "the 'base quantity level' (the average of the quantity of subsidized export of sugar during the base period 1986-1990) was 1,612,000 tones and this quantity level would be

India, Jamaica, Kenya, Madagascar, Malawi, Mauritius, St. Kitts and Nevis, Swaziland and Zimbabwe to join the consultations. In the dispute WT/DS266, Australia, Barbados, Belize, Canada, Colombia, Congo, Côte d'Ivoire, Fiji, Guyana, India, Jamaica, Kenya, Madagascar, Malawi, Mauritius, St. Kitts and Nevis, Swaziland and Zimbabwe requested to join the consultations. On 24 October 2002, the EC informed the DSB that it had accepted the requests of Australia, Barbados, Belize, Canada, Colombia, Congo, Côte d'Ivoire, Fiji, Guyana, India, Jamaica, Kenya, Madagascar, Malawi, Mauritius, St. Kitts and Nevis, Swaziland and Zimbabwe to join the consultations. *European Community – Export Subsidies on Sugar* (2005), WTO Doc. WT/DS 283/R (Panel Report), online: WTO <<http://docsonline.wto.org/gen. search/asp>> [*EC – Sugar III*].

progressively reduced to 1,273,500 tones in the year 2000.” According to the EC, this was an indication of its limitation for export subsidies. The panel stated that the footnote did not constitute a reduction in subsidization and, besides, it was in conflict with *AoA* Arts. 3, 8, 9.1 and 9.2 (b) (iv). The EC alleged in the appeal that “there is no rule of law giving the *Agreement on Agriculture* precedence over provisions in a Member’s schedule.”⁴²⁵

The Appellate Body confirmed the panel’s decision and stated that there was no indication that footnote 1 involved “any EC commitment to ‘limit’ subsidization of exports of sugar.”⁴²⁶ The AB rejected the EC’s argument that *AoA* Art. 3.3 did not require a Member to schedule both budgetary outlay and quantity commitments regarding export subsidies listed in Art. 9.1 and noted that the reference in Article 3.3 to “budgetary outlay *and* quantity commitment levels” suggested that the drafters intended that both types of commitments must be specified.⁴²⁷

Finally, the AB declared that footnote 1 could not prevail over any provision of the *AoA*. It quoted *AoA* Art. 8, which stated that Members were prohibited from providing export subsidies that were not consistent with the *AoA* and the commitments in its schedules, Therefore, export subsidization had to be in accordance with Art. 8, and the schedules and should prevail over footnote 1. Furthermore, *AoA* Art. 21 confirms the precedence of the *AoA*.⁴²⁸ The decision of the AB was that footnote 1 did not contain both quantity and budgetary commitments and that they were not being reduced according to the commitments in the EC’s schedule. For this reason,

⁴²⁵ *EC – Exports Subsidies on Sugar supra* note 359 at para. 165.

⁴²⁶ *Ibid.* at para. 174.

⁴²⁷ *Ibid.* at para. 200.

⁴²⁸ *Ibid.* at para. 222.

they were inconsistent with *AoA* Arts. 3.3 and 9.1 and, consequently, inconsistent with *AoA* Art. 8.⁴²⁹

The AB also addressed the panel's decision that export subsidization of one specific type of sugar⁴³⁰ involved a) "payments," because it was being sold at prices below its average total cost of production; (b) subsidies that were for export and (c) "payments" "financed by virtue of governmental action," according to *AoA* Art. 9.1 (c). The panel reached this decision because it found a link and a clear nexus between the financing of the payments and governmental action. The EC completely controlled the sugar supply and management.⁴³¹

The panel followed the decision in *Canada – Dairy, Canada – Dairy (Article 21.5 – New Zealand and US) and Canada – Dairy (Article 21.5 – New Zealand and US II)*, where the interpretation was that "payments on the export of an agricultural product that are financed by virtue of governmental action" was a mechanism or process by which financial resources were provided by the government or any private party. "By virtue of" meant that a "nexus" or a "link" should exist between the governmental action and the financing of payments. The AB found that all these undertakings existed in these types of EC export subsidies for sugar and, therefore, upheld the panel's decision.⁴³²

Finally the Appellate Body condemned the EC under DSU Art. 3.8, which presumes nullification and impairment if a Member has acted inconsistently with a covered agreement.⁴³³ The EC tried to allege that the "complainants had no expectations of improved competitive

⁴²⁹ *Ibid.* at para. 224-225.

⁴³⁰ *Payments in the form of below cost C beet sales to C sugar producers/exporters. Ibid.* at para. 230.

⁴³¹ "The European Communities, according to the Panel, controls virtually every aspect of domestic beet and sugar supply and management." *Ibid.* at para. 231.

⁴³² *Ibid.* at para. 233-237.

⁴³³ DSU Art. 3.8 states that "[i]n cases where there is an infringement of the obligations assumed under a covered Agreement, the action is considered *prima facie* to constitute a case of nullification or impairment."

opportunities that would come from the EC reducing its exports of C sugar.”⁴³⁴ The AB stated that the fact that the complainants could not expect the EC to take any measure to reduce its exports of the C sugar was not sufficient to rebut the presumption of nullification or impairment. According to the AB, the EC had to demonstrate that there was no adverse trade effect resulting from their export subsidies in sugar in order to rebut this presumption. Because the EC was not able to prove the lack of an adverse trade effect, the AB declared that their export subsidies were inconsistent with DSU Art. 3.8, which meant that they nullified or impaired the benefits of the complainants under the *AoA*.⁴³⁵

In August 2005, complainants asked the DSB for the establishment of a DSU Art. 21.3 panel, because the parties were not able to reach an agreement about a determined period of time for implementation of the panel and AB decisions. In October, arbitration was circulated, establishing that a reasonable period of time would be 12 months and three days, expiring in May 2006. In a separate meeting in September 2005, complainants expressed their concerns about the EC’s decision to increase exports of sugar by almost two million tonnes, which would have an impact on their exports of the product. However, in June 2006, in the fourth year after the dispute started, the complainants informed the DSB that each country had reached an agreement with the EC under DSU Arts. 21 and 22.⁴³⁶

The fourth case was *US – Upland Cotton*, which will be analyzed in further detail in the next section of this study because of its relevance in being the first case to challenge agricultural subsidies when the Peace Clause was expiring. There were just two countervailing duty disputes

⁴³⁴ *EC – Exports Subsidies on Sugar supra* note 359 at para. 296.

⁴³⁵ *Ibid.* at para. 300.

⁴³⁶ DSU Art. 21 establish measures for surveillance of implementation of recommendations and rulings and Art. 22 regulates compensation and the suspension of concessions. It means the Agreement between EC and Australia, Brazil and Thailand involved compensations and surveillance of the panel and AB decisions. *EC – Export Subsidies on Sugar supra* note 359 at 120-121.

during the peace period. The first was only a consultation by Canada about the initiation of a countervailing duty investigation by the US Department of Commerce in 1998 regarding live cattle from Canada. Canada alleged that the investigation was inconsistent with the *SCM Agreement*, did not represent American domestic industry and the subsidies applied were under *de minimis* cap. The dispute did not go further.⁴³⁷

The second case was *Mexico – Olive Oil*.⁴³⁸ In 2006, the EC requested consultations regarding definitive countervailing duties imposed by Mexico on imports of olive oil from the Community. The EC alleged, among other reasons, that the imposition violated the Peace Clause, because Mexico had not exercised “due restraint,” as *AOA* Art. 13 (c)(i) required.

The panel looked for definitions to determine the meaning of “due restraint” and reached the conclusion that it was a “proper, regular and reasonable demonstration of self-control, caution, prudence and reserve.” The panel concluded that there was no reason to conclude that Mexico had not acted with “due restraint” when it imposed countervailing duties. The first reason given by the panel was that it was not necessary to initiate a consultation prior to initiation, so it rejected the EC’s argument that an initiation with no consultation would be lack of “due restraint.” The panel also found that there was neither lack of “self-control” nor “material retardation” when the countervailing measures were applied.⁴³⁹

In this case, even though the complainant was able to overcome the “due restraint” requirement for the challengeability of export subsidies, the panel recommended that Mexico bring its measures into conformity with the *SCM Agreement*.⁴⁴⁰ That was the reason that, on

⁴³⁷ WTO, *United States – Countervailing Duty Investigation with Respect to Live Cattle from Canada, Request for Consultation by Canada*, WTO Doc. WT/DS167/1, G/L/302, G/SCM Agreement/D31/1, G/AoA/GEN/34 (1999) online: WTO <http://docsonline.wto.org/gen_search.asp> at 1.

⁴³⁸ *Mexico – Olive Oil* *supra* note 320.

⁴³⁹ *Ibid.* at paras. 7.70-7.79.

⁴⁴⁰ According to the panel, Mexico had acted inconsistently with *SCM Agreement* Arts. 11.11, 12.4.1 and 15.1. *Ibid.* at 7.249-255.

December 11, 2008, Mexico informed the DSB that a domestic court had ordered Mexican investigating authorities to remove the countervailing duties imposed on olive oil from the EC. The dispute was settled by a publication in the *Official Journal of the Mexican Federation* about the elimination of the disputed measures.⁴⁴¹ In the sole case of countervailing duty on agricultural subsidies that reached the phase of report, the respondent had to withdraw its measures.

Out of only eight cases on the challengeability of agricultural subsidies during nine years of the peace period, three were only consultations and did not go further. Four were highly complex cases, and one of them has not been resolved so far.⁴⁴² This is a clear indication that the shield of the Peace Clause worked effectively to avoid challenges to agricultural subsidies.

The special situation of *US – Upland Cotton* will be analyzed next.

II.4.1 The *United States – Subsidies on Upland Cotton* (DS 267)

The government of Brazil filed consultations with the US about its agricultural subsidization of upland cotton in September 2002. This case will be analyzed in further detail in this section because it was the first WTO decision to address the provisions of the Peace Clause before it expired and continued after its expiration. A possible decision in this case could be that the extension of the Peace Clause could restrain the challengeability of agricultural subsidies under the *SCM Agreement*. For this reason, the panel and the AB report also provided some guidance on the relationship among the *SCM Agreement*, *GATT 1994* and *AoA*. The panel held that the Peace Clause did not impede Brazil's claims under the *SCM Agreement*, which helped to

⁴⁴¹ WTO, *Mexico – Definitive Countervailing Measures on Olive Oil from the European Communities*, online: WTO < http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds341_e.htm>.

⁴⁴² See footnote 410.

define how to apply the *SCM Agreement* provisions on challengeability to agricultural subsidies as regulated in the *AoA*.

Furthermore, the panel addressed several legal issues concerning agricultural subsidization that helped to define the limits of challengeability for agricultural subsidies after the expiry of the Peace Clause.⁴⁴³ It was the first time the WTO dispute settlement system analyzed the extent to which decoupled income support could come under the “cloth” of green box measures and whether export credit guarantee programs could be waived from agricultural subsidy regulations.

The *US – Upland Cotton* case was filed in the context of the launch of the Doha Round in the Fourth WTO Ministerial Conference in Qatar. The Doha Round started a new round of negotiations in the WTO, focusing on new commitments for trade in agriculture and consolidating a shift⁴⁴⁴ of the traditional epicenter of agricultural negotiations. The Declaration of the Ministerial Meeting was determined on the elimination of all forms of export subsidies and substantial reductions in domestic support that distorted trade.⁴⁴⁵

While cotton had always been an important product for the economic health of southern American families,⁴⁴⁶ more recently, it had become an important commodity for small, poor economies in Africa. Therefore, the discussion on subsidies for American cotton was, in fact, an important debate on the relationship between agricultural subsidization and poverty. This debate

⁴⁴³ For this reason, the case was not only of practical relevance, but also presented some original legal issues to WTO dispute settlement. Karen H. Cross, “King Cotton, Developing Countries and the ‘Peace Clause’: the WTO’s US – Cotton Subsidies Decision” (2006) 10 JIEL 55 at 65 [Cross, “King Cotton”].

⁴⁴⁴ See Annex IV.

⁴⁴⁵ WTO, *Doha Ministerial Declaration*, WTO Doc. WT/MIN(01)/DEC/1 (20 Nov. 2001), online: WTO <http://www.wto.org/english/thewto_e/minist_e/min01_e/mindecl_e.htm#agriculture> [*Doha Ministerial Declaration*].

⁴⁴⁶ Cross, “King Cotton” *supra* note 443 at 18.

contributed to creating the Cotton Sub-Committee under the *July 2004 Package* at the November 19, 2004, meeting of agricultural negotiations.⁴⁴⁷

Below, the reasons for the novelty of the case will be proffered.

II.4.1.1 The Novelty of the Case

The *US – Upland Cotton* was a landmark case for the following reasons. It was the first WTO case that held that an agricultural subsidy had caused “significant prejudice” to the interests of another WTO Member.⁴⁴⁸ While *Indonesia – Autos*⁴⁴⁹ had also found that subsidy measures had caused “significant prejudice” to the respondent, that dispute was not about agriculture.

The cotton dispute was also the first one to challenge American export credit guarantees given to agricultural products, which was illegal under the *AoA* and *SCM Agreement*. These export credit guarantees were declared illegal by the panel and the AB for all agricultural products, not only for those provided to cotton.⁴⁵⁰

The dispute also condemned the self-attributed green box nature of some US subsidies (production flexibility contract and direct payment). Currently, any subsidy that distorts production can be challenged in the WTO system, but this was the first green box subsidy condemned by the WTO. The panel decided that the US’s self-declared, purportedly green

⁴⁴⁷ WTO, *The July 2004 Package and August Decision. After the Framework: Modalities*, online: WTO <http://www.wto.org/english/tratop_e/agric_e/negs_bkgnd23_julypack_e.htm> at 75 [*The July 2004 Package*].

⁴⁴⁸ Steinberg, “Peace Clause” *supra* note 7 at at 390.

⁴⁴⁹ *Indonesia – Autos supra* note 234.

⁴⁵⁰ The WTO panel held that the export credit guarantee program was prohibited for all but 12 US agricultural products exempted in the Uruguay Round negotiations. *US – Upland Cotton supra* note 330.

support in the way of direct payments given to farmers were not, in fact, green measures, because they were distorting production.⁴⁵¹

The panel and the AB also condemned for the first time agricultural subsidies that caused “serious prejudice” under *SCM Agreement* Articles 5 and 6, which helped to define the boundaries for the challengeability of agricultural subsidies under the *SCM Agreement* after the expiry of the Peace Clause. The decision in this case created a roadmap for future challenges to domestic and export subsidies on agriculture. It was also the first WTO dispute involving serious prejudice to use an econometric analysis as a tool for quantifying the amount of serious prejudice created by domestic and export agricultural subsidies.

The econometric analysis in this case was needed to prove that the US was subsidizing its cotton production. Brazil’s allegation was that the subsidized cotton was displacing cotton exports from Brazil in third-party markets. The US alleged that other factors, such as price, were displacing Brazilian cotton exports. Therefore, the economist hired by the government of Brazil to do the econometric calculations, the American Professor Daniel Sumner, former Assistant Secretary of Economics at the United States Department of Agriculture (USDA), developed econometric models to prove that American cotton subsidies were displacing Brazilian cotton exports.

Though it had to be proven that American cotton exports had displaced Brazilian exports, several factors can influence a country’s decision to buy cotton from one exporter or another. Some factors are economic, such as price; others are commercial, such as quality and time to deliver. Some subjective factors can also influence a buyer’s preference for one specific seller.

The role of econometrics is to give empirical content to economic relations by formulating economic models in testable forms and to estimate and test those models.⁴⁵²

⁴⁵¹ *US – Upland Cotton supra* note 14 at 288.

Therefore, in a subsidy case, one of the econometrics applications is that of identifying which factors influence the buyer's decision and calculate how much each factor interfered in the decision.

For example, in a subsidy case, the demand relationship is relevant, which is the relationship between the price of the commodity and the quantities of the commodity that will be bought for that specific price, is relevant. According to economic theory, an increase in the price would lead to a decrease in the quantity demanded, which holds other variables constant so as to isolate the relationship of interest.

A mathematical equation can be written to describe this relationship between quantity (Q) and other variables such as price, income or others (o). Normally a random term is added (E) because of the imprecision of the theoretical method:⁴⁵³

$$Q = \alpha_0 + \alpha_1 Price + \alpha_2 Income + E$$

This formula can calculate the relationship between the factors that influenced the quantity bought of an agricultural product. The answer can lead to a conclusion that the economic theory of price and quantity demanded is not working in the specific case analyzed. This conclusion could indicate that external or unknown factors could be influencing the decision to buy rather than the variable price.

Other formulas would have to calculate whether subsidies could be considered as one of these external or unknown factors that distorted the normal relation between price and quantity

⁴⁵² Pesaran, M. Hashem, *Econometrics. The New Palgrave: A Dictionary of Economics*, v. 2 (Hampshire: Palgrave Macmillan, 1987) at 8-22.

⁴⁵³ Maddala, G. S., *Introduction to Econometrics*, 2nd ed. (New York: Macmillan, 1992) at 4.

bought. Regression analysis can estimate the unknown parameters α , β_1 and β_2 in an economic model. This illustrates the complexity of the calculations, and most of the formulas have the random term “E,” which means that there will always be a certain level of uncertainty in the conclusions.

The source chosen for the figures to be used in the econometric formulas is highly significant, which is why the source of the econometric data was so contentious in the case. In the *US – Upland Cotton*, Professor Sumner used the Food and Agricultural Policy Research Institute’s [FAPRI] model, because it was the one that the USDA used for econometric calculations of agricultural subsidies. His methodology was contested by the US, but accepted by the panel. Eventually, however, FAPRI (a governmental funded institution jointly run by Iowa State University and the University of Missouri at Columbia established by Congress in 1984) refused to reveal the parameters of its models, and therefore, the model could not be used further in the case. However, at this point, the Professor Sumner’s model had already been accepted by the panelists.⁴⁵⁴

This process in the case illustrates not only the complexity of econometrics, but also how difficult it is to establish the parameters and data that will be calculated according to different models and methodologies that can always be questioned by the parties. In *US – Upland Cotton*, the reasoning in the case deviated from legal to economic arguments for a significant amount of time.

The case was also relevant because, for many years, heavy agricultural subsidization was a common practice among several WTO Members, because of, among other reasons, the complex legislation for challengeability and the higher thresholds for challengeability brought in

⁴⁵⁴ Goldberg, Ray A., Lawrence, Robert & Milligan, Katie “Brazil’s WTO Cotton Case: Negotiation through litigation” *Article N9-905-405* (Boston: Harvard Business School Publishing, 2004) at 243 n.11.

by the Uruguay Round agreements. However, this case proved that it was possible to challenge agricultural subsidies after the Uruguay Round, even with high thresholds for challengeability, as is going to be seen in the next section.

II.4.1.2 The Figures in the case

The data from the USDA proved that the US was subsidizing cotton at such a level that it surpassed the value of crops themselves. According to the USDA, in 2001–2002, the US government paid almost \$4 billion in subsidies for cotton crops that were worth slightly more than \$3 billion, a subsidization rate of 129.3 percent.⁴⁵⁵

Between August 1999 and 2003, the total production costs of US producers were, on average, 77% above the cotton market prices. Despite the high profits accrued by American farmers in 1999, 2001 and 2002, cotton prices hit the lowest level ever recorded. In the spring of 2002, the price of cotton plunged to 29 cents per pound—far below the past 20-year average of 72 cents per pound. Nevertheless, American production of cotton increased during that time from 13.1 million acres during the period 1998–2001 to 15.5 million acres in 2002. In the face of record low prices, US production reached the second highest level of production ever in 2001–2002.⁴⁵⁶ The consequence of these production records, in spite of the low market prices, was a significant increase in US cotton exports. The American market share of cotton exports increased from 17% in 1998–1999 to 42% in 2002–2003, even though the value of the US dollar increased

⁴⁵⁵ Memorandum for a Press Briefing from Scott D. Andersen, leading lawyer from the law firm that worked in the case on behalf of the Brazilian government, *Factual and Legal BackGround Info to the WTO Panel Decision in the Cotton Dispute*, (February 2005)(Washington, SdA, 2005) at 4 [*Memo Cotton Case, Andersen*].

⁴⁵⁶ *Ibid.* at 5.

by about 154%.⁴⁵⁷ In normal conditions, the American products would have become more expensive and less competitive in the world trade market.

On the other hand, the exports of more efficient and lower-cost producers, such as African countries and Brazil, hit record low levels. While US exports were doubling, the share of the West African cotton producers in the export market dropped from 15% to 11%, even though cotton production costs in Brazil and Africa were significantly lower than the US average.⁴⁵⁸

Econometric studies⁴⁵⁹ were used in the cotton case to prove that US production and exports increased as a result of subsidies that distorted prices and created unfair competition in the international cotton market. These studies demonstrated that during the period 1999–2002 US production of cotton increased on average by 29%, while exports increased on average by 41%. At the same time, cotton prices decreased on average by 12.6%, or 6.5 cents per pound, in the international market.⁴⁶⁰

With all the evidence pointing to subsidization at higher levels than authorized, the panel held that US subsidies for cotton were incompatible with the *AoA* and the *SCM Agreement* provisions.

II.4.1.3 The Panel

⁴⁵⁷ *Ibid.*

⁴⁵⁸ *Ibid.*

⁴⁵⁹ *Ibid.* at 6.

⁴⁶⁰ The FAPRI model used by Professor Daniel Sumner in this WTO case was based in production, price and trade effects of US agricultural policy and was developed by the University of Missouri and Iowa State University. *Ibid.* p. 5.

On September 27, 2002, due to the evidence on US agricultural subsidy programs, Brazil requested clarifying consultations with the US on the legality of several US commodity support programs.⁴⁶¹

When consultations failed, on February 6, 2003, Brazil requested the establishment of a panel to review alleged prohibited and actionable subsidies provided to US producers, users and/or exporters of upland cotton. Brazil made claims regarding marketing loan program payments, user marketing (Step 2) payments, production flexibility contract payments, market loss assistance payments, direct payments, counter-cyclical payments, crop insurance payments, production flexibility contract payments, market loss assistance payments, direct payments, counter-cyclical payments, crop insurance payments, cottonseed payments, export credit guarantees and the FSC Repeal and Extraterritorial Income Exclusion Act of 2000 (Public Law 106-519) (the "ETI Act of 2000").⁴⁶²

At the same time, Brazil requested that it be able to start procedures under *SCM Agreement* Art. 7, paragraph 4, which provides specific remedies for actionable subsidies. As a consequence, Brazil asked the US, under *SCM Agreement Annex V*, paragraph 2, for information

⁴⁶¹ These were the American subsidies challenged by Brazil at the panel hearing and in the recourse to the AB: a) marketing loan programs payments, which involved interim financing to domestic producers to facilitate the gradual distribution of the commodity throughout the year; b) production flexibility contract payments, which involved support to producers based on historical acreage and yields (not related to current prices of cotton); c) market loss assistance payments, which involved ad hoc emergency and supplementary assistance provided to producers for compensating potential losses should commodity prices fall under a certain level; d) direct payments, which were support to producers based on historical acreage and yields (not related to current prices of cotton); e) counter-cyclical payments, which were support to producers based on historical acreage and yields (related to the current price of cotton); f) crop insurance payments, which involved insurance coverage to producers for losses due to natural disasters and market fluctuations; g) cottonseed payments, which involved ad hoc emergency and supplementary assistance provided to first handlers and producers of cottonseed; h) user marketing payments ("Step 2" programs), which were marketing certificates or cash payments to domestic users and exporters of upland cotton when certain US cotton pricing benchmarks were exceeded; i) export credit guarantee measures ("GSM 102", "GSM 103" and "SCGP"), which were guarantees to US exporters against the risk of not being paid, in the event that the foreign bank failed to pay under the foreign bank letter of credit or the importer failed to pay under the importer obligation and j) export subsidies under the ETI Act of 2000, which were tax breaks (non-taxation of a portion of extraterritorial income accruing from upland exports). See generally in *US – Upland Cotton supra* note 14.

⁴⁶² *Ibid* at 1.

about the existence and amount of subsidization provided for upland cotton. This *SCM Agreement* provision regulates the procedures to obtain information from the government of the subsidizing Member to establish the existence and amount of subsidization, as well as the necessary information to analyze the adverse effects caused by the subsidized product.⁴⁶³ The US argued that some of the measures were domestic support measures that were exempt from challengeability according to *AoA* paragraphs (a) and (b).⁴⁶⁴

On May 23, 2003, the panel⁴⁶⁵ was established by the WTO Director-General.⁴⁶⁶ Brazil alleged that the US had violated the Peace Clause's provisions, because its cotton subsidies were higher than in the 1992 base period.⁴⁶⁷ In a briefing to the panel, the US countered that the Peace Clause had waived agricultural subsidies from all legal actions, which included legal processes, suits or legal steps to establish a claim. Therefore, to go through the substantive claims of the panel,⁴⁶⁸ the US asserted that the panel should first verify whether the Peace Clause allowed American agricultural subsidies to be challenged.

⁴⁶³ *SCM Agreement* Annex V paragraph 2 provides:

In cases where matters are referred to the DSB under paragraph 4 of Article 7, the DSB shall, upon request, initiate the procedure to obtain such information from the government of the subsidizing Member as necessary to establish the existence and amount of subsidization, the value of total sales of the subsidized firms, as well as information necessary to analyze the adverse effects caused by the subsidized product. This process may include, where appropriate, presentation of questions to the government of the subsidizing Member and of the complaining Member to collect information, as well as to clarify and obtain elaboration of information available to the parties to a dispute through the notification procedures set forth in Part VII [footnotes omitted].

⁴⁶⁴ This was the second time in the history of the WTO that a Member has requested Annex V procedures to obtain information related to a claim of serious prejudice and market disruption originated from subsidizing practices. It was the first one in agriculture. The only time this procedure was used was in *Indonesia – Autos*, after requests by the US and EC.

⁴⁶⁵ Thirteen countries participated in this case as third parties: Argentina, Australia, Benin, Canada, Chad, China, the European Communities, India, New Zealand, Pakistan, Paraguay, Chinese Taipei and Venezuela. That was the first time in the WTO history until the date of the establishment of the panel that so many third parties had participated in a WTO dispute.

⁴⁶⁶ The panelists were the following: chair, Dariusz Rosati from Poland; Mario Matus from Chile; and Daniel Moulis from Australia. *US – Upland Cotton supra* note 330 at 2.

⁴⁶⁷ Under *AoA* Article 13 (the Peace Clause) subsidies on agriculture were exempt from actions based on paragraph 1 of Article XVI of GATT 1994 or Articles 5 and 6 of the Subsidies Agreement, since such measures did not grant support to a specific commodity in excess of that decided during the 1992 marketing year.

⁴⁶⁸ *US – Upland Cotton supra* note 330 at 19.

Brazil, on the other hand, declared that the panel should address substantive claims along with the Peace Clause's examination. In June 2003, the panel decided to determine whether or not the US was in violation of the Peace Clause prior to ruling on Brazil's substantive claims.⁴⁶⁹

In September, the panel declined "to make findings at this stage as to whether measures raised in this dispute satisfy the conditions in *AoA* Article 13."⁴⁷⁰ The panel then held that it would proceed to examine Brazilian substantive claims. It is of note that, if the panel had decided to first rule on the Peace Clause's limits for challengeability, not only would the case take longer but the main Brazilian allegations could be jeopardized.

Regarding the main substantive claims, Brazil argued that US cotton subsidies were illegal under the WTO rules, because they had driven down world prices for cotton and had given US producers an unfair share of world exports. According to the data provided by the USDA, the US government was using several different types of subsidies for cotton production. These subsidies were distributed as follows:

- a) \$898 million in marketing loan payments guaranteeing producer revenues of \$0.52 per pound for current cotton production;
- b) \$1,309 million in counter-cyclical payments triggered by prices below \$0.6573 per pound and based on updated historical acreage and yield data.
- c) \$194.1 million in crop insurance subsidies for cotton.
- d) \$415 million in Step-2 payments to exporters and domestic users of US cotton.
- e) \$617 million in direct payments of 6.667 cents per pound to cotton farmers based on updated historical acreage and yield data.
- f) \$50 million in cottonseed payments to cover the costs of ginning (processing raw cotton).
- g) Export credit guarantees facilitating the export of \$349 million worth of cotton to selected developing countries."⁴⁷¹

⁴⁶⁹ *Ibid.* at 21.

⁴⁷⁰ *Ibid.* at 26.

⁴⁷¹ *Memo Cotton Case, Andersen supra* note 455 at 4.

In December 2003, the US refused to give further information about their cotton subsidies programs. It stated that “the release of planted acreage information associated with a particular farm, county, and state number was confidential and could not be released under United States domestic law, the Privacy Act of 1974.”⁴⁷² As a result of this American refusal to give required information, the panel decided to draw adverse inferences about US subsidization.⁴⁷³

The US initially⁴⁷⁴ asserted that the United States Department of Agriculture [USDA] had not collected any such payment information and, as a result, could not calculate the amount of payments received by US cotton producers. Later, the USDA sent the required information.⁴⁷⁵

Brazil also received the assistance of the Environmental Working Group (EWG), a Washington, D.C.– based non-governmental organization (NGO) that provided the USDA’s subsidies data. Because of this information, the panel received a very close approximation of the amount of subsidies received by US cotton producers. Only⁴⁷⁶ after five requests and significant pressure from the panelists, did the American government disclose⁴⁷⁷ specific farm data that proved US subsidies were in fact coupled to cotton production.

⁴⁷² *US – Subsidies on Cotton supra* note 330 at 32.

⁴⁷³ *Ibid.* at 35.

⁴⁷⁴ The date of the allegation was October 2002.

⁴⁷⁵ An intern of the law firm with headquarter in Washington D.C. that worked for Brazil in the dispute gave a telephone call the USDA and asked if they had information concerning American agricultural support programs. The USDA employee not only confirmed the existence of the numbers, but also sent them directly to the intern. Interview of Roberto Azevedo, the former chief of the Brazilian Mission at WTO in Geneva (16 October 2004) in Brazilian Ministry of Foreign Affairs, Brasilia at Annex V.

⁴⁷⁶ On 3 March 2004, the United States submitted the data requested by the Panel on 3 February 2004, as well as its comments on Brazil's 18 February 2004 comments. The document was entitled "Response of the United States of America to the Panel's February 3, 2004 Data Request, as Clarified on February 16, 2004", submitted together with a CD-ROM. On paragraph 31, the United States designated the data submitted as confidential pursuant to paragraph 3 of the Panel's working procedures. *US – Upland Cotton supra* note 330 at 36 and n. 92.

⁴⁷⁷ In a similar situation in *Canada – Aircraft*, the panel declined Brazil's request to draw "adverse inferences" from Canada's refusal to supply the information on a debt financing for aircraft on the grounds of commercial confidentiality. The panel argued that there was not sufficient basis for making such inferences. Panel Report, *Canada – Measures Affecting the Export of Civilian Aircraft* (1999), WTO Doc. WT/DS70/R, online: WTO <[http://docs.wto.org/gen. search/asp](http://docs.wto.org/gen.search/asp)> at n. 621 [*Canada – Aircraft*].

After getting all of the needed information to proceed, Brazil still had to overcome the Peace Clause's barrier to the challengeability of the challenged subsidies.

II.4.1.4 The Peace Clauses' Barrier to Challengeability

Because the case started in September 2002, before the Peace Clause had expired, the complainants had to overcome the clause's shield against the challengeability of agricultural subsidies. Firstly, there was the part of the Peace Clause that hindered the challengeability of any domestic subsidy falling within the green box during the implementation period.⁴⁷⁸ If a subsidy could be classified under the green box (which meant that it was minimally production- and trade-distorting and de-coupled from production), then it could be granted without being subject to any challenge.

Brazil and the US disagreed as to whether US Direct Payments [DP] under the 2002 Farm Act and the "Production Flexibility Contract Payments" [PFC] under the 1996 Farm Act were green box subsidies. Brazil alleged that they were not green box subsidies because they were not completely de-linked from production, as *AoA* Annex II requires. The panel decided PFC and DP were not domestic support measures that conformed to the provisions and requirements of the *AoA* Art. 13(a) that regulate green box measures and, therefore, could be challengeable.⁴⁷⁹

The Peace Clause also prohibited trade-distorting non-green box subsidies (amber and blue) unless the amount of subsidies granted was equal to or below the levels of 1992. Therefore, any Member that exceeded the 1992 levels could have its subsidies challenged under the serious

⁴⁷⁸ See *AoA* Article 13(a).

⁴⁷⁹ *US – Upland Cotton supra* note 330 at 347.

prejudice provisions of the *SCM Agreement*. The panel held that 1999–2002 US cotton support measures⁴⁸⁰ had granted support to a specific commodity in excess of that decided during the 1992 marketing year. Therefore, it had not satisfied the conditions of the Peace Clause,⁴⁸¹ and, as such, were not exempt from actions based on allegations of serious prejudice⁴⁸² and adverse effects⁴⁸³ contained in the *SCM Agreement*.

The Peace Clause also prohibited any Member from challenging export subsidies so long as the Member did not subsidize at higher levels than permitted under the *AoA* Article 13(c). However, the United States had not negotiated the right to provide export subsidies during the Uruguay Round. For this reason, the panel held that both US cotton export subsidies—the Step 2 export subsidies and export credit guarantees—challenged by Brazil had violated the US export subsidy commitments under the WTO Agriculture Agreement.⁴⁸⁴

Furthermore, the panel found that export credit guarantees for all but 12 other agricultural products had also violated the WTO Agriculture Agreement and, for this reason, could not have the protection of the Peace Clause. The summary of the decision on the export subsidies was as follows:⁴⁸⁵

- a) United States export credit guarantees⁴⁸⁶ are export subsidies applied in a manner which results in circumvention of United States' export subsidy

⁴⁸⁰ Specifically the marketing loan program payments, user marketing (Step 2) payments to domestic users (and not to exporters), production flexibility contract payments, market loss assistance payments, direct payments, counter-cyclical payments, crop insurance payments, and cottonseed payments. *Ibid.* at VIII 8.1(b).

⁴⁸¹ *AoA* Paragraph (b) of Article 13.

⁴⁸² *GATT 1994* Art. XVI, para. 1 or *SCM Agreement* Art. 6.

⁴⁸³ *SCM Agreement* Art. 5.

⁴⁸⁴ *US – Upland Cotton supra* note 330 at 348.

⁴⁸⁵ *Ibid.* at 348-349.

⁴⁸⁶ United States export credit guarantees under the General Sales Manager 102 ("GSM 102"), General Sales Manager 103 ("GSM 103") and Supplier Credit Guarantee Program ("SCGP") and other unscheduled agricultural products supported under the programmes as rice.

commitments, within the meaning of *AoA* Article 10.1⁴⁸⁷ being therefore inconsistent with *AoA* Article 8.⁴⁸⁸ As they do not conform fully to the export competition commitments of the *Agreement on Agriculture*,⁴⁸⁹ they do not satisfy the condition of the Peace Clause⁴⁹⁰ and, therefore, are not exempt from actions based on allegations of serious prejudice, adverse effect or allegations based on article 3⁴⁹¹ of the *SCM Agreement*;

- b) United States export credit guarantees are provided by the United States government at premium rates which are inadequate to cover long-term operating costs and losses of the programmes, and therefore constitute *per se* prohibited export subsidies;⁴⁹²
- c) however, according to the panel, Brazil had not made a prima facie case that exports of unscheduled agricultural products not supported under the programmes and other scheduled agricultural products do not conform fully to the provisions of Part V of the *Agreement on Agriculture*. Then, the Panel recognized that these subsidies were exempted from actions based on serious prejudice⁴⁹³ and Article 3 of the *SCM Agreement*;
- d) section 1207(a) of the FSRI Act of 2002⁴⁹⁴ provided for user marketing (Step 2) payments to exporters of upland cotton is an export subsidy⁴⁹⁵ inconsistent with the United States' obligations under the *Agreement on Agriculture*;⁴⁹⁶ therefore do not satisfy the condition of the Peace Clause that exempt from actions based on allegations of serious prejudice, adverse effect or allegations based on article 3 of the *SCM Agreement*, being prohibited under the

⁴⁸⁷ *AoA* Article 10.1 states that “[e]xport subsidies not listed in paragraph 1 of Article 9 shall not be applied in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments; nor shall non-commercial transactions be used to circumvent such commitments.”

⁴⁸⁸ *AoA* Article 8 states that “[e]ach Member undertakes not to provide export subsidies otherwise than in conformity with this Agreement and with the commitments as specified in that Member’s Schedule.”

⁴⁸⁹ *AoA* provisions of Part V.

⁴⁹⁰ *AoA* Art. 13(c).

⁴⁹¹ *SCM Agreement* Article 3.1 establishes that “[e]xcept as provided in the *Agreement on Agriculture*, the following subsidies, within the meaning of Article 1, shall be prohibited: (a) subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I; (b) subsidies contingent, whether solely or as one of several other conditions, upon the use of domestic over imported goods. 3.2 A Member shall neither grant nor maintain subsidies referred to in paragraph 1” [footnotes omitted].

⁴⁹² *SCM Agreement* Arts. 3.1(a) and 3.2.

⁴⁹³ *GATT 1994* Art. XVI

⁴⁹⁴ Farm Security and Rural Investment Act of 2002 (the “FSRI Act of 2002”); Public Law 107-171. *US – Upland Cotton supra* note 330 at n. 264.

⁴⁹⁵ *AoA* Article 9.1(a) list some export subsidy subject to reduce commitments “(a) the provision by governments or their agencies of direct subsidies, including payments-in-kind, to a firm, to an industry, to producers of an agricultural product, to a cooperative or other association of such producers, or to a marketing board, contingent on export performance.”

⁴⁹⁶ Inconsistent under *AoA* Arts. 8 and 3.3 that follows: “[s]ubject to the provisions of paragraphs 2(b) and 4 of Article 9, a Member shall not provide export subsidies listed in paragraph 1 of Article 9 in respect of the agricultural products or groups of products specified in Section II of Part IV of its Schedule in excess of the budgetary outlay and quantity commitment levels specified therein and shall not provide such subsidies in respect of any agricultural product not specified in that Section of its Schedule.”

SCM Agreement.⁴⁹⁷ The FSRI for domestic users is also prohibited under the *SCM Agreement*;⁴⁹⁸

Brazil proved that the US had given subsidies for cotton at a higher level than was allowed by the Peace Clause and had wrongly classified distortive measures as non-distortive, which violated the Peace Clause. Therefore, the panel held that the US subsidy measures—marketing loan program payments, user marketing (Step 2) payments, MLA payments⁴⁹⁹ and CCP payments⁵⁰⁰ and CCP payments⁵⁰¹ – indicated significant price suppression in the same world market within the meaning of the *SCM Agreement*.⁵⁰² This constituted serious prejudice⁵⁰³ to the interests of Brazil; however, the panel ruled that Brazil had not established that the effect of PFC payments, DP payments and crop insurance payments was significant price suppression

⁴⁹⁷ Prohibited under *SCM Agreement* Arts. 3.1(a) and 3.2.

⁴⁹⁸ *Ibid.*

⁴⁹⁹ The panel defined MLA payments as market loss assistance payments provided to recipients of production flexibility contract payments through *ad hoc* legislation as additional assistance to producers to make up for losses caused by low commodity prices. Market loss assistance payments were proportionate to the production flexibility contract payments made to the recipient, and the amount paid depended on the amount allocated to market loss assistance payments for the relevant crop year. Accordingly, eligibility criteria for the market loss assistance payments were, essentially, the same as for the production flexibility contract payments.” *US – Upland Cotton supra* note 330 at paras. 7.216-7.217.

⁵⁰⁰ The panel defined MLA payments as market loss assistance payments were provided to recipients of production flexibility contract payments through *ad hoc* legislation as additional assistance to producers to make up for losses caused by low commodity prices. Market loss assistance payments were proportionate to the production flexibility contract payments made to the recipient, and the amount paid depended on the amount allocated to market loss assistance payments for the relevant crop year. Accordingly, eligibility criteria for the market loss assistance payments were, essentially, the same as for the production flexibility contract payments”. *US – Upland Cotton supra* note 330 at paras. 7.216-7.217.

⁵⁰¹ The Panel defined CCP Payments as counter-cyclical payments supplement, for covered commodities, direct payments and any payments made under the marketing loan program. The eligibility requirements and planting flexibility requirements are the same as under the direct payment program, and they are also dependent on base acres. Counter-cyclical payments supplement producer incomes by filling the gap between, on the one hand, the market price and payments under the marketing loan program and the direct payments program and, on the other hand, a target price established for upland cotton at 72.4 cents per pound. *Ibid.* at paras. 7.223-7.226.

⁵⁰² *SCM Agreement* Art. 6.3(c) states that “the effect of the subsidy is a significant price undercutting by the subsidized product as compared with the price of a like product of another Member in the same market or significant price suppression, price depression or lost sales in the same market.”

⁵⁰³ *SCM Agreement* Art. 5(c) states that “no Member should cause, through the use of any subsidy referred to in paragraphs 1 and 2 of Article 1, adverse effects to the interests of other Members, i.e.,: ... (c) serious prejudice to the interests of another Member” [footnote omitted].

in the meaning of the *SCM Agreement*.⁵⁰⁴ It also found some US subsidy measures⁵⁰⁵ constituted serious prejudice⁵⁰⁶ to the interests of Brazil because they increased America's world market share⁵⁰⁷ under the *SCM Agreement*.

Furthermore, according to the panel, Brazil had made a prima facie case that ETI Act of 2000 export subsidies were inconsistent with the *AoA*,⁵⁰⁸ which meant these subsidies were not exempt from actions based on allegations of serious prejudice⁵⁰⁹ or on Article 3 of the *SCM Agreement*.

Based on these findings, the panel recommended that the US bring the measures listed in paragraphs 8.1(d)(i)⁵¹⁰ and 8.1(e)⁵¹¹ of the panel report into conformity with the *AoA*. It also required the US to withdraw the prohibited subsidies listed in paragraphs 8.1(d)(i), 8.1(e) and 8.1(f)⁵¹² of the panel report without delay. With respect to the marketing loan program payments, user marketing (Step 2) payments, MLA payments and CCP payments, the panel

⁵⁰⁴ *SCM Agreement* Art. 6.3(c).ASDF

⁵⁰⁵ The panel listed the following measures (i) user marketing (Step 2) payments to domestic users and exporters; (ii) marketing loan programme payments ; (iii) production flexibility contract payments; (iv) market loss assistance payments; (v) counter-cyclical payments; (vi) crop insurance payments; (viii) cottonseed payments for the 2000 crop; and (ix) legislative and regulatory provisions currently providing for the payment of measures in (i), (ii), (v), (vi) and (viii) above. *US – Upland Cotton supra* note 330 at para. 7.1107.

⁵⁰⁶ Serious prejudice within the meaning of *SCM Agreement* Art. 5(c).

⁵⁰⁷ World market share within the meaning of *SCM Agreement* Art. 6.3(d) that establishes “the effect of the subsidy is an increase in the world market share of the subsidizing Member in a particular subsidized primary product or commodity as compared to the average share it had during the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted” [footnote omitted].

⁵⁰⁸ *AoA* Arts. 10.1 and 8.

⁵⁰⁹ *GATT 1994* Article XVI.

⁵¹⁰ The measures listed in para. 8.1(d)(i) were American export credit guarantees under the GSM 102, GSM 103 and SCGP export credit guarantee programmes: (i) in respect of exports of upland cotton and other unscheduled agricultural products supported under the programmes, and in respect of one scheduled product (rice). WTO Report, *US – Upland Cotton supra* note 330 at 348.

⁵¹¹ The measures listed in para. 8.1(e) were section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to exporters of upland cotton. *Ibid.* at 349.

⁵¹² The measures listed in 8.1(d)(i), 8.1(e) and 8.1(f) were section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to domestic users of upland cotton”. *Ibid.*

noted that, pursuant to Article 7.8 of the *SCM Agreement*, the US was under an obligation to “take appropriate steps to remove the adverse effects or ... withdraw the subsidy.”⁵¹³

It was clear in the panel’s decision that agricultural subsidies could be challenged under the *SCM Agreement* if they distort trade and do not comply with the *AoA*, even with the shield of the Peace Clause. Both parties appealed.

II.4.1.5 The Appeal

In October 2004, the US filed a Notice of Appeal and on October 28, after the deadline of 05:00 PM,⁵¹⁴ the US filed its appellant's submission. In November 2004, Brazil filed another appellant's submission and in the same month both Brazil and the US filed their appellees’ submissions.⁵¹⁵

On November 16, Argentina, Australia, Canada, China, the European Communities and New Zealand individually filed third participant's submission, and Benin and Chad filed a joint third participant’s submission. India, Pakistan, Paraguay, Venezuela, and the Separate Customs

⁵¹³ *Ibid.* at para. 8.3(d).

⁵¹⁴ Brazil complained that the US was recurrently missing the deadline to submit their petitions:

Pursuant to Rule 21(1) of the *Working Procedures*. In a letter dated 1 November 2004, Brazil, without requesting action by the Appellate Body, drew attention to the failure by the United States to submit its appellant's submission in a timely fashion. Brazil observed that the United States' appellant's submission was submitted on 28 October 2004 after the deadline of 5:00 p.m. that had been established by the Division in the *Working Schedule* issued pursuant to Rule 26 of the *Working Procedures*. *US – Upland Cotton supra* note 14 at n. 19.

⁵¹⁵ *Ibid.* at 7.

Territory of Taiwan, Penghu, Kinmen and Matsu notified the Appellate Body of their intention to appear at the oral hearing.⁵¹⁶

The oral hearing in this appeal was held from December 13 to 15. The participants and third participants (with the exception of Pakistan, Paraguay, and Venezuela) presented oral arguments and responded to questions posed by the Members of the division hearing the appeal.

Because of the complexity and diversity of this case, Brazil and the US agreed that additional time was needed for the issuance of the AB report. The deadline agreed to by Brazil and the US was no later than March 3, 2005,⁵¹⁷ which was duly met by the AB.

The AB report affirmed the panel's report, adding only a few changes. It rejected all 19 US appeal allegations and confirmed all the key findings of the report. The AB affirmed the panel's finding that the US subsidization of cotton during 1999–2002 exceeded the 1992 level for four consecutive years and, therefore, should be removed.

One important decision by the AB, not stated in the panel report, was that it did not exclude the possibility that challenged non-“price-contingent” subsidies could have some effect on production and contribute to “price suppression.” The AB decision had implications not only for the subsidies given to US products, but also for some subsidies given by the EC to their farmers. As for the marketing, loan and counter-cyclical payments, the AB affirmed that they caused serious prejudice and were directly tied to production.⁵¹⁸ The AB also affirmed the panel's decision that Step 2 export subsidies for upland cotton were prohibited subsidies and highly trade distorting.⁵¹⁹

⁵¹⁶ *Ibid.*

⁵¹⁷ *Ibid.* at 8.

⁵¹⁸ *Ibid.* at 289.

⁵¹⁹ *Ibid.* at 289-290.

The AB affirmed the panel's finding that the US export credit guarantee subsidies⁵²⁰ were prohibited and had to be eliminated as well. It confirmed the panel's rejection of US arguments that these export credit guarantees were not export subsidies. It also rejected US arguments that export credit guarantees were not subject to WTO rules, which meant that the US would have to eliminate the subsidies for these products by July 1, 2005.⁵²¹

It found that it was illegal for the US to provide export credit guarantees for more than 190 different types of fruits and vegetables, along with lamb, pork, cotton, soybeans, rice, wood products, fruit juices and even wine. These products represented more than half by value of all products in the ECG's. Only the cotton crops received \$1.6 billion of ECG financing..⁵²²

Furthermore, the AB affirmed the panel's finding that the US Direct Payment Program was coupled with production, because it fostered the production of particular crops.⁵²³ This meant that US direct payment subsidies could not be placed in the green box and, thus, were considered to be distorting measures classified as amber and blue box support measures. The decision made the US vulnerable to WTO challenges in regard to limits in total subsidization for amber box subsidies.

The AB affirmed the decision by the panel to apply *SCM Agreement* rules on serious prejudice to agricultural subsidies. This opened up possibilities for potential future challenges of US and EC domestic subsidies and facilitated future disputes brought up by non-subsidizing countries. However, the US has not yet complied with the AB rulings.

⁵²⁰ *Ibid.* at 292-293.

⁵²¹ On August 18, 2006, Brazil filed a petition under DSU Article 21.5 asking for the US to comply with the decisions of the case. On June 20 2008 the AB Report was adopted and, basically held that the US had to comply with the decisions of the original panel.

⁵²² *Memo Cotton Case, Andersen supra* note 455 at 12.

⁵²³ *US – Upland Cotton supra* note 14 at 121-123.

II.4.1.6 Compliance

In order to comply with the AB report, the US would have to withdraw its declared illegal subsidies programs or change its statutes. The US has eliminated Step 2 prohibited export subsidies, but all other subsidies declared incompatible by the panel remain. As stated above, the panel found that the marketing loan, CCP and Step 2 domestic subsidies caused serious prejudice to Brazilian interests.

The only way for the US to remedy this would be to change its laws. Generally, WTO rulings for non-export subsidies give to losing parties a long period of time to make legislative changes. The US is currently postponing this legislative modification. There were no significant changes in the Farm Bill 2008 and, therefore, on August 18, 2006, Brazil requested the establishment of a DSU 21.5 panel for compliance.

The panel found that the US had failed to comply with its obligation under *SCM Agreement* Art. 7.8 to take appropriate steps to remove or withdraw subsidies. Regarding export credit guarantees issued after July 1, 2005, the panel determined that the US had acted inconsistently with *AoA* Art. 10.1 and 8, because it had circumvented its commitments under the *Agreement* and under *SCM Agreement* Art. 3.1(a) and 3.2.

On July 4, 2005, Brazil asked the DSB for authorization to suspend concessions or other obligations under *SCM Agreement* Art. 4.10 and DSU Art. 22.2⁵²⁴ because a reasonable period of time to comply with the decision had expired on July 1st, 2005. Regarding prohibited subsidies, on July 5, 2005, both parties notified the DSB that they had agreed to apply the procedures

⁵²⁴ If a Member fails to bring inconsistent measures into compliance in a period of time determined in Art. 21 para. 3, negotiations must be initiated to reach a satisfactory compensation within 20 days after the date of expiry of the reasonable period of time. If it is not reached, the party that invoked the dispute settlement may request authorization from the DSB to suspend concessions.

outlined in DSU Arts. 21 and 22. Regarding actionable subsidies, on October 6, 2005, Brazil requested the suspension of concessions under *SCM Agreement* Art.7.10 and DSU 22.2. Brazil also asked for the procedures outlined in DSU Art. 22.6,⁵²⁵ to be applied for both actionable and prohibited subsidies, but by mutual agreement, they were suspended.

The DSU 22.2 panels remained for prohibited and actionable subsidies and on August 31, 2009, the two decisions were circulated. Regarding prohibited subsidies, the arbitration determined that Brazil could suspend concessions or other obligations under any WTO Annex 1A agreements at a level not to exceed the amount of US\$147.4 million for 2006 and, for subsequent years, according to the methodology applied by the arbitrator. The same amount was defined annually with respect to the actionable subsidies. The arbitrators also determined that, under specific conditions, Brazil would also be able to suspend obligations under the Agreement on Trade-Related Aspects of Intellectual Property Rights [TRIPS]⁵²⁶ and the General Agreement on Trade and Services [GATS]⁵²⁷.

On November 19, 2009 the DSB authorized Brazil to suspend the application of concessions or other obligations to the US under DSU Art. 22.7.⁵²⁸ On March 8, 2010, Brazil notified the DSB that, from April 7, 2010, onwards, it would increase import duties on certain products imported from the US. Brazil also informed the DSB that it would suspend the application of certain concessions to the US regarding the GATS and TRIPS.

On April 30, 2010, Brazil informed the DSB that it was negotiating a framework agreement with the US and that it would not impose countermeasures before June 21, 2010. On

⁵²⁵ DSU Art. 22.6 establishes that if a Member objects the level of suspension proposed or the procedures of suspension of concessions were not duly followed, the matter can be referred to an arbitration.

⁵²⁶ *WTO Legal Texts supra* note 1 at 321.

⁵²⁷ *Ibid.* at 284.

⁵²⁸ WTO, *United States – Subsidies on Upland Cotton*, online: WTO <http://www.wto.org/english/tratop_e/dispu_e/cases_e/ds267_e.htm>

August 25, Brazil and the US informed the DSB that they had concluded the Framework for a Mutually Agreed Solution to the Cotton Dispute in the World Trade Organization (Framework”). Within this Framework, American domestic subsidy programs as well as credit guarantees program would be reviewed according to a pre-determined schedule. As well, the US had to pay US\$147 million dollars to the Brazilian cotton industry annually. However, on June 6, 2011, the US House of Representatives voted to block the US\$147 million of annual payments to the Brazilian cotton industry.⁵²⁹

The WTO cotton “battle” started almost eight years ago, and the ruling has not been complied with yet. This is one more example of the difficulties that arose in challenging agricultural subsidies during the Peace Clause years and the difficulties in implementing a decision in the WTO dispute settlement system. As stated, the *US – Upland Cotton* case was filed before the Peace Clause expired. However, the decisions proved that the challenged green, non-green and export subsidies were challengeable under the *AoA* and *SCM Agreement* if they distorted trade. The panel and the AB used *SCM Agreement* Art. 3 to condemn export subsidies that complied with the *AoA* requirements . It established that the priority of the *AoA* to verify the compatibility of agricultural subsidies did not prevent challengeability under the *SCM Agreement*, if there were no conflict between the two. The result of the decision is that agricultural subsidies can now be challenged under the *SCM Agreement*, even if they comply with the limits established in the *AoA*, if they cause adverse effects.

The decision not only had legal implications but was also echoed in the Doha Round negotiations. It helped to reinforce the point that agricultural subsidies had to be reduced, which could contribute to Members reducing their level of subsidization and also facilitate the

⁵²⁹ *Ibid.*

negotiations in the Doha Round. If there is no agreement in the Doha Round on agricultural subsidies, and subsidizing Members do not reduce the support levels, agricultural subsidies will most likely be challenged in the WTO dispute settlement system, according to the roadmap of this case.

Scrutinization of the *AoA*, the Peace Clause and the WTO cases on agricultural subsidies has shown that the *AoA* was not the only WTO agreement that interfered with the challengeability of agricultural subsidies after the expiry of the Peace Clause. Therefore, the *SCM Agreement* will be further studied, so that a complete assessment of the framework for the challengeability of agricultural subsidies at the present in the WTO compared with the GATT years can be made.

II.5 The Agreement on Subsidies and Countervailing Measures [*SCM Agreement*]

The *SCM Agreement* used a structure similar to the one used in the TRSC, comparable to 1979 Track I (the multilateral track with international obligations) and Track II (the unilateral track with application of countervailing duties). The TRSC was divided into seven parts, and among them were general provisions, treatment of developing countries, provisions for countervailing measures, dispute settlement and final provisions. The *SCM Agreement* inherited all these parts from the TRSC. The difference was that Track I of the *SCM Agreement* divided up the general provisions to define specific, prohibited and actionable subsidies. The non-actionable subsidy provisions of *SCM Agreement* Art. 8 and 9 have already expired. *AoA* Art. 31 established that “the provisions of Article 8 and Article 9 shall apply for a period of five years, beginning with the date of entry into force of the WTO Agreement.” Therefore, these provisions were valid

from January, 1, 1995, to January, 1, 2001. The *SCM Agreement* also had additional parts on institutions, notification and surveillance and transitional arrangements.

Even though the *SCM Agreement* regulates subsidies in a more detailed way and in a broader landscape, the influence of the TRSC is strong, as will be seen in this section. The core of the *SCM Agreement* is contained within the first five substantive parts. It gives the structure of the *SCM Agreement* subsidy disciplines. Part I established general provisions and defined a subsidy as a financial contribution from a public body that involves a direct transfer of funds, government revenue forgone or not collected, government provision or purchase of goods other than infrastructure or governmental payment to a funding mechanism or any form of income in the sense of Article XVI where a benefit is conferred.

It has been seen that the *AoA* regulated agricultural subsidies in an incomplete manner, because the Doha Round has not finished and there is no definitive agreement on modalities. It can be stated that the *AoA* agricultural boxes defines the substantive limits for the challengeability of agricultural subsidies, and the *SCM Agreement* regulates the procedural limits of the challengeability for all subsidies. This does not mean that the *SCM Agreement* has no substantive provisions but, in fact, means that, regarding the challengeability of agricultural subsidies, the *SCM Agreement* has an important role in establishing the procedural limits of this challengeability.

The *AoA* identifies agricultural subsidies by their nature and classifies them according to their potential distortive effects. The *SCM Agreement* classifies all subsidies according to their level of legality: there are prohibited and actionable⁵³⁰ subsidies. Therefore there is an challengeability zone of confluence between the *AoA* and the *SCM Agreement* as well as the *GATT 1994* that is still valid. The limits of challengeability under the *AoA* were evaluated in the

⁵³⁰ See *supra* note 6.

previous section through the definition of the agricultural boxes. The *SCM Agreement* limits will be evaluated in this section and the confluence zone will be analyzed in the next part of this study.

The *SCM Agreement* created an elaborate procedural system for the challengeability of subsidies, which included the regulation of challengeability with boxes of classification for prohibited and actionable subsidies. It also defined minimum thresholds and some requirements to challenge prohibited and actionable subsidies and tied the concept of serious prejudice to displacement.

II.5.1 Defining Boxes under *SCM Agreement* Challengeability

Parts II and III⁵³¹ of the *SCM Agreement* define two boxes (categories) and certain sub-boxes with some particular exceptions to some of the rules. The lines that separate the different types of subsidies are not totally clear. Part II establishes the regulation of prohibited subsidies and focuses primarily on export subsidies. *SCM Agreement* Annex I has an illustrative list of export subsidies. Subsidies that are contingent upon the required use of domestic, over-imported goods are also included in this prohibited category. There are certain exceptions in the Agreement, including those for developing countries (Part VIII). The agreement states, however, that in case of prohibited subsidies, a Member can challenge them without proving any sort of injury or prejudice. Part III defines actionable subsidies with the statement that “no Member

⁵³¹ There were three categories, but Part IV that regulated non-actionable expired according to the *SCM Agreement* Art. 31.

should cause, through the use of any subsidy ... adverse effects to the interests of another Member.”⁵³²

In short, two categories of subsidies are strictly prohibited: subsidies that are contingent upon export⁵³³ performance and subsidies that are contingent upon the use of domestic over imported goods, the so called import substitution subsidies.⁵³⁴ Actionable subsidies are classified in another category because they can be challenged, but only if they cause material injury to domestic industries.⁵³⁵ In other words, actionable subsidies (e.g., government benefits to a specific enterprise or industry), even if not prohibited, may be challenged under the *SCM Agreement*, if used in a way as to cause “serious prejudice” to the interests of another WTO Member.⁵³⁶ Serious prejudice occurs a subsidy causes significant price suppression in the same market.⁵³⁷

When a government confers a financial benefit on a specific group of producers, this benefit can be considered as a subsidy under WTO rules and, for this reason, may be challenged by another WTO Member if it causes serious prejudice. If a specific subsidy is prohibited, according to Article 4.7 of the *SCM Agreement*, as was seen, the panel has to recommend that the subsidizing Member withdraw the subsidy without delay, and specify a deadline for withdrawal.⁵³⁸ Article 4.7 provides a remedy for prohibited subsidies that is not commonly available in WTO dispute settlement.⁵³⁹

⁵³² See *SCM Agreement* Agreement Part III Article 5 Caput.

⁵³³ See *SCM Agreement* Agreement, Article 3.1(a)

⁵³⁴ See *SCM Agreement* Agreement, Article 3.1(b)

⁵³⁵ See *SCM Agreement* Agreement, Article 15

⁵³⁶ See *SCM Agreement* Agreement, Article 5(c)

⁵³⁷ See *SCM Agreement* Agreement, Article 6.3 (c)

⁵³⁸ See *SCM Agreement* Agreement, Article 4.7.

⁵³⁹ Article 19.1 of the WTO Dispute Settlement Understanding provides that where a panel finds that a measure is inconsistent with a WTO Agreement, the panel simply shall recommend that the measure be brought into conformity with that Agreement.

The rules for injury determination are significantly similar to those for antidumping. The rules set forth in the *SCM Agreement*, analyzed in the next section, add details to the international obligations concerning the determination of subsidies, the procedures of an investigation and the methods for calculating the amount of a subsidy.

II.5.2 Definition of a Subsidy

In order to be actionable under the *SCM Agreement*, a subsidy has to be specific.⁵⁴⁰ The *SCM Agreement* rules that established a definition for subsidies can be considered as an advance, but the requirement of specificity for challengeability raises the threshold for challengeability once again. The *SCM Agreement* filled the gap left by the TRSC, which did not clearly define subsidies. Nevertheless, this definition is not exhaustive, because governments always find new ways to subsidize, and the *SCM Agreement* does not provide a complete list of support measures. This is the reason why some WTO panels helped to define the boundaries of the *SCM Agreement* definition.

The first article of the Agreement defines the word “subsidy.” It must be a financial contribution from the government that confers a benefit on the recipient.⁵⁴¹ It can take the form of a) governmental direct transfer of funds; b) revenue that is forgone or not collected; c) governmental provision of goods or services; or, d) indirect subsidies through a funding mechanism.⁵⁴² The cases analyzed below illustrate that financial contribution can be given in several forms that might not include a direct financial transfer by a government or any entity controlled by the government.

⁵⁴⁰ As seen in the previous section, an export subsidy does need to be specific to be challenged.

⁵⁴¹ See *SCM Agreement* Art. 1.1.

⁵⁴² See *SCM Agreement* Art. 1.1 (a)(1)(i)-(iv).

The concepts “financial contribution” and “public body” have some idiosyncrasies that have to be analyzed. Some WTO panels helped to interpret these concepts. In *Korea – Measures Affecting Trade in Commercial Vessels* [*Korea – Commercial Vessels*], Korea alleged about *SCM Agreement* 1.1 that there was no subsidy when the financial contribution came from individual public bodies or private bodies, because the contribution was decided by creditors’ councils, meetings of interested parties or a court decision. The panel held that “an entity will constitute a ‘public body’ if it is controlled by the government (or other public bodies).” In this case, the panel decided that KEXIM⁵⁴³ was a “public body,” because it was controlled by the Korean government.⁵⁴⁴ Therefore, a subsidy can be given not only directly by a government, but also by an institution controlled by a government.

Regarding the financial contribution by a government within the territory of a Member, in *European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft* [*EC – Aircraft*] the panel stated that when a subsidy involved a direct transfer of funds, the focus had to be on “the existence of a government practice that involves an obligation to make a direct transfer of funds which, in and of itself, is claimed and capable of conferring a benefit on the recipient that is separate and independent from the benefit that might be conferred from any future transfer of funds.” Even though *SCM Agreement* Art. 1.1(a)(1)(i) states that potential direct transfers of funds or liabilities are also subsidies, the *EC – Aircraft* case decided that “potential” does not mean possible transfers to be made in the future.⁵⁴⁵

⁵⁴³ Panel Report, *Korea – Measures Affecting Trade in Commercial Vessels* (2005), WTO Doc. WT/DS273/R, at para. 2.1. adopted 11 April 2005, DSR 2005:VII, 2749 [*Korea – Commercial Vessels*]

⁵⁴⁴ *Ibid* at paras. 7.424-425.

⁵⁴⁵ Panel Report, *European Communities and Certain Member States – Measures Affecting Trade in Large Civil Aircraft* (2010) WTO Doc. WT/DS316/R at 7.302-308 adopted 30 June 2010 circulated to WTO Members 30 June 2010 [adoption/appeal pending] [*EC – Aircraft*]

Regarding the concept of subsidy in *SCM Agreement* Art. 1.1(a)(i), in *Japan – Countervailing Duties on Dynamic Random Access Memory [Japan – DRAMS (Korea)]*, the Appellate Body upheld the panel’s finding that the financial contribution could be given in several forms: loan repayment terms (existing loans, reduction of the interest rates on existing loans and conversion of interest to principal); and debt-to-equity swaps, such as transactions involving “direct transfer(s) of funds” within the meaning of Article 1.1(a)(i) of the *SCM Agreement*.⁵⁴⁶

In *European Communities – Countervailing Measures on Dynamic Random Access Memory Chips from Korea [EC – Countervailing Measures on DRAM Chips]* the panel decided that the challenged subsidy given by Korea involved a direct transfer of funds in the sense of Article 1.1(a)(1)(i).⁵⁴⁷ “This guarantee constituted a financial contribution in the sense of Article 1.1(a)(1)(i) of the *SCM Agreement*.”⁵⁴⁸ Also the panel held that the purchase of corporate bonds was a direct transfer of funds under Article 1.1(a)(1)(i) and, for this reason, was a financial contribution.⁵⁴⁹

Regarding the concept of forgone revenue in *SCM Agreement* Art. 1.1(a)(1)(ii), the *US – FSC* panel held that the determination of whether the revenue that is otherwise due is forgone if it involves a comparison between the “fiscal treatment being provided by a Member in a particular situation and the tax regime otherwise applied by that Member.”⁵⁵⁰ In *Indonesia –*

⁵⁴⁶ Panel Report, *Japan – Countervailing Duties on Dynamic Random Access Memory* (2007), WTO Doc. WT/DS336/R at paras. 246-256 adopted 17 December 2007, as modified by Appellate Body Report WT/DS336/AB/R, DSR 2007:VII, 2805 [*Japan – DRAMS (Korea)*].

⁵⁴⁷ Panel Report, *European Communities – Countervailing Measures on Dynamic Random Access Memory Chips from Korea* (2005), WTO Doc. WT/DS299/R at para. 7.69 adopted 3 August 2005, DSR 2005:XVIII, 8671 [*EC – Countervailing Measures on DRAM Chips*].

⁵⁴⁸ *Ibid.* at paras. 7.85-87.

⁵⁴⁹ *Ibid.* paras 7.88-93.

⁵⁵⁰ *US – FSC supra* note 354 at paras. 4.41-100.

Autos the panel determined that “tariff and sales tax exemptions in question represent government revenue forgone within the meaning of Article 1.1(a)(1)(ii).”⁵⁵¹

Regarding *SCM Agreement* Art. 1.1(a)(1)(iii), which stated that a subsidy could be a governmental “provision of goods or services other than general infrastructure, or purchases goods,” the *EC – Aircraft* panel determined that “general infrastructure” refers to “infrastructure that is not provided to, nor for the advantage of, only a single entity or limited group of entities, but rather is available to all, or nearly all, entities”⁵⁵² In *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada* [*US – Softwood Lumber IV*] the Appellate Body Report analyzed the concept of “good” and reached the conclusion it should not be read so as to exclude tangible items of property.”⁵⁵³

Regarding the definition of the concept of benefit in *SCM Agreement* Art. 1.1(a)(2), even though *SCM Agreement* Art. 14 gives guidance on countervailing duties, this concept is not clear in the *SCM Agreement* regarding subsidies. In *Canada – Measures Affecting the Export of Civilian Aircraft* [*Canada – Aircraft*] the Appellate Body decided that there was a benefit when there was an advantage for the recipient receiving the subsidy from the government or from a public body when compared with what it would have received in the market in normal conditions.⁵⁵⁴ This case set up the definition of a benefit by using market parameters. In *US – Upland Cotton*, the panel held that a benefit must place the “recipient” in a better position than it otherwise would have been in the market.”⁵⁵⁵

⁵⁵¹ *Indonesia – Autos supra* note 234 at 14.155.

⁵⁵² *EC – Aircraft supra* note 545 at 7.1015.

⁵⁵³ Appellate Body Report, *United States - Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada* (2004), WTO Doc. WT/DS257/AB/R at para. 50 adopted 17 February 2004, DSR 2004:II, 571. [*US – Softwood Lumber IV*].

⁵⁵⁴ Appellate Body Report, *Canada – Measures Affecting the Export of Civilian Aircraft* (1999), WTO Doc. WT/DS70/AB/R adopted 20 August 1999, DSR 1999:III, 1377 [*Canada – Aircraft*].

⁵⁵⁵ *US – Upland Cotton supra* note 14 at 7.118

In *Mexico – Definitive Countervailing Measures on Olive Oil* [*Mexico – Olive Oil*] the panel established that Art. 1.1(b), which states that a benefit must be provided in order for a subsidy to be characterized as one in *SCM Agreement* Art. 1.1(a)(2), did not clearly establish the requirements to accurately calculate the amount of the benefit “accruing to a particular recipient in a countervail investigation” and, for this reason, held that “the European Communities has not established that Mexico acted inconsistently with its obligations under Article 1.1 of the *SCM Agreement* by failing to conduct a pass-through analysis in the olive oil investigation.” First, the panel clarified that, if no benefit is conferred in the sense of *SCM Agreement* Art. 1.1(b), then “no subsidy exists” and noted that the EC did not argue that a benefit had not been provided. Instead, the allegation was that Mexico had not properly calculated in quantitative amounts the benefit that was linked to exports of olive oil.

In response to the EC’s allegation, the panel stated that it had not identified in *SCM Agreement* Art. 1.1 “any language specifically relating to how the amount of the benefit is to be calculated in a countervail investigation.”⁵⁵⁶ For this reason, the panel determined that the EC had not established that Mexico had “acted inconsistently with its obligations under Article 1.1 of the *SCM Agreement*.” To support this decision the panel remembered the conclusion in *United States – Countervailing Measures on Certain EC Products* [*US – Certain EC Products*] which stated that the “recipient of the benefit might be different from the recipient of the financial contribution, and a subsidy can be bestowed directly or indirectly, and in respect of production, manufacture or export of a product.”⁵⁵⁷ The conclusion of the panel in *Mexico – Olive Oil* was that “it was not necessary to identify the particular recipient or recipients of the benefit, and the

⁵⁵⁶ *Mexico – Olive Oil* *supra* note 320 at para. 7.151.

⁵⁵⁷ Appellate Body Report, *United States – Import Measures on Certain Products from the European Communities* (2001), WT/DS165/AB/R, at paras. 110-113 adopted 10 January 2001, DSR 2001:I, 373 [*US – Certain EC Products*] quoted in *Ibid.* at 7.152

particular manner in which a subsidy is bestowed, in order to determine that a benefit has been conferred, and that therefore a subsidy exists, within the meaning of Article 1.1(b).”

The *SCM Agreement* generally defined what a subsidy was; however, the market is always creating new support policies and new ways to subsidize. Debt-to-equity swaps and other indirect support also can be considered as subsidies, as the cases demonstrated, which means that the *SCM Agreement* does not have a definitive list of practices that could be considered as subsidies, but it gives some guidance and sets out principles to determine what a support measure is. The limits and requirements were determined with the help of the WTO panel and AB decisions, as was seen in *Mexico – Olive Oil*.

SCM Agreement Art. 1.1 (a)(2) states that any form of income or price support in the sense of *GATT 1994* Art. XVI must be considered a subsidy as well. Therefore, the *SCM Agreement* defines what a subsidy is but clearly does not exclude the possibilities for subsidization regulated in the *GATT 1994*. Actually, in another reference to the *GATT 1994*, footnote 1 of the *SCM Agreement* states that, according to *GATT 1994* Art. XVI (and Note to Article XVI) and the provisions of Annexes I through III of the *SCM Agreement*, duties or tax exemptions for exported products or the remission of them shall not be considered as a subsidy.

II.5.3 The Specificity Test

The “specificity” regulated in Article 2 is a requirement for the application of a trade remedy (countervailing duty) or any international procedure (e.g., the WTO dispute settlement system). It should be noted that the concept of specificity was developed with the purpose of preventing non-trade distortive subsidies from being part of the concept developed in the *SCM*

Agreement. This means that, when a subsidy is widely available in the economy of a Member, a possible distortion as a consequence of the subsidization is presumed not to occur, since a subsidy is a legitimate instrument of governmental policy if it does not violate the WTO rules.

According to the *SCM Agreement*, specificity is found when a subsidy is given to an enterprise, an industry, or group of enterprises or industries.⁵⁵⁸ All prohibited subsidies defined as such in *SCM Agreement* Part II are specific as well as subsidies limited to certain enterprises located in a geographical region under the jurisdiction of the granting authority.⁵⁵⁹

Distortive subsidies must be submitted to the restrictive measures of the *SCM Agreement*. There is a presumption that, if a support is broadly given and is part of an economy, it is not distortive, but if it is specific to an enterprise, an industry, a group of enterprises or a group of industries, it distorts trade. Therefore, there are four sorts of specificity according to the *SCM Agreement*: enterprise, industry, regional and prohibited.⁵⁶⁰

It should be mentioned that any subsidy considered to be prohibited according to the criteria mentioned in *SCM Agreement* Art. 3 (contingent upon export performance or upon the use of domestic over-imported goods) was considered to be specific under *SCM Agreement* Art. 2. In *Korea – Commercial Vessels*, the panel found that the discussed subsidies were specific on the basis of *SCM Agreement* Art. 2.3, in which prohibited subsidies are deemed to be specific. The panel rejected Korea's argument that "such subsidies are not specific for the purpose of the EC's actionable subsidy claims, since the EC failed to argue any specificity other than Article 2.3 of the *SCM Agreement*." The panel found that "a subsidy that is specific under Article 2.3 (as result of export contingency) is specific for the purpose of both Part II (prohibited export

⁵⁵⁸ See *SCM Agreement* Art. 2.1.

⁵⁵⁹ See *SCM Agreement* Art. 2.2 and 2.3.

⁵⁶⁰ WTO, *Subsidies and Countervailing Measures – Overview, Agreement on Subsidies and Countervailing Measures* ("*SCM Agreement* Agreement") online: WTO <http://www.wto.org/english/tratop_e/scm_e/subs_e.htm>

subsidy) and Part III (actionable subsidy) claims.”⁵⁶¹ This decision reinforced the fact that if a subsidy is prohibited under *SCM Agreement* Art. 3, it is consequently specific, which means that specificity does not need to be proved.

SCM Agreement Article 2.1 covers both *de jure* and *de facto* specificity. *De jure* specific subsidies are given to a certain group of enterprises if there are no clear and objective conditions that define their eligibility. Their amount is determined by law, regulation or another official document.⁵⁶² In *EC – Aircraft* the panel decided that the analyzed subsidy was specific because it represented “a unique transfer of funds at below-market interest rates to one particular company.”⁵⁶³ In *US – Upland Cotton*, specificity was proved because the challenged subsidies were limited to some segments of the US economy or industry or subgroups of industries that grow certain crops.⁵⁶⁴

In *United States – Continued Dumping and Subsidy Offset Act of 2000* [*US – Offset Act (Byrd Amendment)*] the panel stated that in order to verify if a subsidy can be *de jure* specific under *SCM Agreement* Art. 2.1(a), it is necessary to verify if it is given to “an enterprise or industry or group of enterprises or industries” according to the chapeau of Art. 2.1. The panel stated that Mexico did not argue that the subsidy in question “explicitly limits access to offset payments to an ‘enterprise or industry or group of enterprises or industries’” and, for this reason, decided that the challenged subsidies were not specific according to the meaning of *SCM Agreement* Art. 2.1(a).⁵⁶⁵

⁵⁶¹ *Korea – Commercial Vessels* *supra* note 542 at paras. 7.512-514.

⁵⁶² See *SCM Agreement* Art. 2.1 (a) and (b).

⁵⁶³ *EC – Aircraft* *supra* note 545 at 7.497

⁵⁶⁴ *US – Upland Cotton* *supra* note 14 at para. 7.1122.

⁵⁶⁵ Panel Report, *United States – Continued Dumping and Subsidy Offset Act of 2000*, (2003) WT/DS217/R, WT/DS234/R, at 7.116 adopted 27 January 2003, as modified by Appellate Body Report WT/DS217/AB/R, WT/DS234/AB/R, DSR 2003:II, 489 [*US – Offset Act (Byrd Amendment)*].

De facto subsidies, even though they have the appearance of non-specificity according to the criteria of *SCM Agreement* Art. 2.1 (a) and (b), can be deemed as specific if other factors are taken into account. These factors are predominant use by certain enterprises, disproportionately large amounts of subsidies given and the way that discretion has been exercised by a national authority in granting the subsidy. Variables such as the length of time the subsidization is given for are considered to identify a *de facto* subsidy.⁵⁶⁶ For example, a neutral subsidy can be specific if used very often by certain enterprises.

In *United States – Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada* [*US – Softwood Lumber IV*], the panel held that the stumpage programs were, in fact or *de facto*, specific because they were given “to a limited group of wood product industries” and, therefore, came within the contemplation of the definition outlined in Article 2.1(c). For this reason, the panel rejected the claim that the imposition of countervailing duties on the basis of the specificity determination have to “deliberately limited” access to the subsidy to certain enterprises.⁵⁶⁷

It was seen in this section that the *SCM Agreement* established rules to define the concept of specificity because only specific subsidies can be challenged under the *SCM Agreement*. The panels defined the boundaries of this concept and corroborated that export subsidies were deemed to be specific under *SCM Agreement* Art. 2.3 and that *de jure* subsidies of Art. 2.1(a) had to be verified first according to the chapeau of this article.

It should be noted that “specificity” in the *SCM Agreement* is a proscriptive test and not an “effect” test for the verification of the existence of a subsidy. This means that if a subsidy is

⁵⁶⁶ See *SCM Agreement* Art. 2.1 (c).

⁵⁶⁷ *US – Softwood Lumber IV supra* note 553 at paras. 7.106-125.

specific, it is prohibited. This is the reason why exports prohibited in *SCM Agreement* Art. 3 are deemed to be specific.

The concept of specificity was applied to all parts of the *SCM Agreement*, which included regulations on countervailing duties. Even though *GATT 1994* Art. XVI and the TRSC did not have a clear definition of a subsidy, they also did not have the requirement of specificity for challengeability. As has been seen, this requirement was used by defendants to try to avoid condemnation of their subsidizing practices. Therefore, the definition of a subsidy can be viewed as a legislative improvement, but the requirement of specificity once again raises thresholds for challengeability. The concepts of serious prejudice and displacement under the *SCM Agreement* will be analyzed below.

II.5.4 Serious Prejudice and Displacement

Another important requirement for the challengeability of subsidies under the *SCM Agreement* is the “serious prejudice” test in Part III of the *SCM Agreement*, which effectively brought in provisions that added new thresholds for challengeability for the concept of a subsidy established in *GATT 1947* Art. XVI. *SCM Agreement* Footnote 13 states that “serious prejudice to the interests of another Member” is used in the same sense as it was used in paragraph 1 of Article XIV of *GATT 1947* and includes the threat of serious prejudice. The *SCM Agreement* elaborated this concept, imposing more specific standards for subsidy challengeability.

The basis for challengeability in the GATT years was Art. XVI, which stated that any subsidy maintained by a party that directly or indirectly increased exports or reduced imports would be notified. In any case, if the subsidy caused or threatened to cause serious prejudice to the interests of any other contracting party, the possibility of limiting the subsidy has to be discussed. The key concept for challengeability is serious prejudice. It has been seen in section I.2.1 that the concept of serious prejudice during the GATT years was not directly linked with price suppression until the TRSC was established.

Part III (articles 5, 6 and 7) of the *SCM Agreement* regulates actionable subsidies. Article 5 defines the basic idea of actionability, stating that a Member's subsidy cannot cause an adverse effect to another. Adverse effects comprise three specific situations: injury, nullification or impairment of benefits and serious prejudice. Injury is a concept that was more clearly defined, because it has been used in trade remedies, such as anti-dumping and countervailing measures. Nullification or impairment of benefits was also a clear concept in *GATT 1947* Arts. II and XXIII 1(b). The serious prejudice concept was not completely explained in *GATT 1947* Article XVI, and for this reason, *SCM Agreement* Art. 6 clearly elaborated further on the concept.

In *Korea – Commercial Vessels*, the European Communities alleged that serious prejudice had occurred “on the basis of price suppression/depression”. They alleged that Korean subsidies on three particular types of commercial vessels (container ships, product/chemical tankers and liquefied natural gas carriers [LNGs]) enabled Korean shipyards to reduce their prices or keep their prices stable despite strong increases in demand and production costs, which otherwise would have led to price increases.

The panel did not agree with the European Communities and held that “nothing in the evidence and arguments had demonstrated that the aggregate effect of the subsidized transactions

is significant” price suppression/depression. Therefore, the panel rejected the EC claim that the subsidized transaction had seriously prejudiced the EC’s interests by causing significant price suppression.⁵⁶⁸

In order to reach such a finding, the panel made a detailed analysis of the legal framework to be applied in determining “whether a subsidy has caused serious prejudice to the interests of a Member,” which is relevant to this study. First, the panel stated that *SCM Agreement* Art. 5 identified three possible kinds of adverse effects: a) injury, b) nullification or impairment of benefits from *GATT 1994* Art. II bindings and c) serious prejudice, which the EC had used to based its claim on.

The panel noted that Art. 6 provided specific guidance concerning the establishment of serious prejudice” in the sense of Art. 5(c), which states that “serious prejudice in the sense of paragraph (c) of Article 5 arises in any case (c) the effect of the subsidy is a significant price undercutting ... or significant price suppression, price depression, or lost sales in the same market.”

With regard to the meaning of “price suppression” and “price depression,” the panel concluded that “trends in prices would not themselves constitute price suppression or price depression.” For Korea, serious prejudice “must have to do primarily with that Member’s prices for the product in question,” while the EC “states that Korean prices have been suppressed or depressed by subsidies, and, in turn has suppressed or depressed ‘world’ ship prices and EC shipyards’ prices.”

The panel stated that “whereas it is ‘relatively simple’ to show that prices have declined, it is likely to be more difficult to show that prices should not have decreased, or should have

⁵⁶⁸ *Korea – Commercial Vessels supra* note 543 paras. 10.258-268.

increased by more than they did.” For the panel, the analysis “concerns what the price movements for the relevant ships *would have been* in the absence of the subsidies at issue.”⁵⁶⁹

The European Communities argued that nothing in Article 6.5(c) would preclude defining “world” market as the “same market” for purposes of a price suppression/price depression analysis. On the other hand, Korea alleged that “the same market can only refer to a national market, not to the world market.”⁵⁷⁰ The panel addressed this issue, stating that Art. 6.3(c) “places no geographic limitations on the concept of the same market.” This view was consistent with that in *EC – Sugar Exports (Australia)*, *EC – Sugar Exports (Brazil)* and *US – Upland Cotton*.⁵⁷¹

When the panel addressed the issue of “serious prejudice ... may arise,” it stated that there was a cross-reference when the *chapeau* of Art. 6.3 referred to “serious prejudice in the sense of Article 5(c).” This cross-reference is strong evidence that the situations listed in Art. 6.3(a)-(d) are serious prejudice in the sense of Art. 5(c).

The panel then considered the negotiating history of the provision to reach a conclusion. Within this framework, the panel stated that “the question to be answered in respect of the affirmative link between subsidies and prices is, in the case of alleged price depression, whether in the absence of the subsidies prices for ships would not have declined, or would have declined by less than was in fact the case.”⁵⁷² In this regard, the panel noted that the *US – Upland Cotton* panel “analyzed other possible causal factors, with a view to determining whether such factors would have the effect of attenuating the causal link or of rendering not significant the effect of the subsidy.” The panel considered this approach to be logical and appropriate and applied the

⁵⁶⁹ *Ibid.* at paras. 7.536-537.

⁵⁷⁰ *Ibid.* at paras. 7.562-563.

⁵⁷¹ *Ibid.*

⁵⁷² *Ibid.* at paras. 7.631-614.

same rationale in *Korea – Commercial Vessels* to determine that nothing demonstrated that the effect of the subsidized transactions⁵⁷³ was significant “price depression/suppression.”

Therefore, the panel rejected the EC claim that the subsidized transactions “seriously prejudiced the EC’s interests” by causing significant price depression/suppression.⁵⁷⁴ As is shown by the panel’s analysis, several *SCM Agreement* concepts had to be addressed, such as “price depression/suppression” and “world market.” This case exemplifies that the *SCM Agreement* provisions on subsidy regulation raised the thresholds for actionability higher than those found in *GATT 1947*. In *Korea – Commercial Vessels*, the EC could not prove that Korean subsidies distorted trade and were illegal under *SCM Agreement* Arts. 5 and 6. Even though it is not an agricultural case, it helps to demonstrate the new and more complex levels for actionability brought by the *SCM Agreement*. The case helped to elucidate the limits of actionability for actionable subsidies under *SCM Agreement* Arts. 5 and 6.

SCM Agreement Art. 6’s quantitative limitation of 5%⁵⁷⁵ for the determination of serious prejudice has expired, but *SCM Agreement* Art. 6.2 (which has not expired) states that serious prejudice cannot be found if the measure in question does not cause one of the effects listed in *SCM Agreement* 6.3: if there is a) displacement in the nation; b) displacement in a third country; c) significant price undercutting or price suppression, price depression or lost sales; and d) an increase in the world market share. All of these concepts were already in the Tokyo Round Subsidies Code.⁵⁷⁶

⁵⁷³ The Panel identified three subsidized APRGs and no subsidized PSLs; for product/chemical tankers, the Panel identified two subsidized APRGs and 24 subsidized PSLs; for container ships, the Panel identified eight subsidized APRGs and 21 subsidized PSLs. *Ibid.* at paras. 7.681-685, 7686-689 and 7.691-694.

⁵⁷⁴ *Ibid.* at paras. 7.684-684.

⁵⁷⁵ The calculation of the total ad valorem subsidization was determined by the value of the product as the total value of the recipient firm’s sales in the most 12-month period, for which sales data is available, preceding the period in which the subsidy is granted. *SCM Agreement* Annex IV 2.

⁵⁷⁶ The period of three years established in *SCM Agreement* 6.3(d) for determining an increase in the market share was also the same stated in the Tokyo Round Subsidies Code Article 10:2(c).

Item d has particular relevance for agriculture, because the whole provision states that serious prejudice is found when:

“the effect of the subsidy is an increase in the world market share of the subsidizing Member in a particular subsidized primary product or commodity as compared to the average share it had during the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted.”⁵⁷⁷

This provision differs from Art. 10.1 of the TRSC in some aspects, but one point is especially relevant. While TRSC Art. 10.1 established that an actionable agricultural subsidy was characterized by the subsidizing country’s having more than an equitable share of world export trade in the product, the *SCM Agreement* suppressed the polemical term “equitable.” It determined that an “increase in the world market share of the subsidizing Member” would be enough.

The TRSC had established that the subsidy that had given more than an equitable share of a product to a signatory had to cause displacement in order to be challengeable.⁵⁷⁸ The *SCM Agreement* actually made challengeability possible either by displacement,⁵⁷⁹ price undercutting⁵⁸⁰ or an increase in the “world market share” for the subsidizing Member.⁵⁸¹ A shallow analysis of the provision would give the false impression that the *SCM Agreement* lowered the requirements for challengeability. This conclusion would be based on the fact that, purportedly, an increase in the market share of any agricultural product regulated by the *SCM Agreement* would be easier to prove than the “more than equitable share of world export trade” established by the *GATT 1947* and the TRSC. If the *SCM Agreement* does not require

⁵⁷⁷ See *SCM Agreement* Art. 6.3(d).

⁵⁷⁸ See TRSC Art. Article 10:2(a).

⁵⁷⁹ See *SCM Agreement* Art. 6.3(a) and (b).

⁵⁸⁰ See *SCM Agreement* Art. 6.3(c).

⁵⁸¹ See *SCM Agreement* Art. 6.3 (d).

displacement to prove an increase in the market share and the TRSC did require it, the *SCM Agreement* purportedly would have made challengeability easier.

However, the *SCM Agreement* did not reduce the actionability requirements in this specific case. It is a false impression. *SCM Agreement* Art 6.4 determines that the purpose of paragraph 3(b) – displacement – should include a change in the relative shares of the market. Then, the article clarifies what “change” means: a) an increase in the market share of the subsidized product, b) the market share remains constant in a circumstance where it would have declined and c) the market share declines, but at a slower rate. This explanation of what a change in the market share means is similar to the *GATT 1994* and TRSC’s concept of more than an equitable share of world export trade. The consequence is that the complainants in WTO cases have to prove displacement in order to challenge an agricultural subsidy under *SCM Agreement* Art. 6.3, as the analysis of the cases in this section will demonstrate.

The *GATT 1994* did not use the concept of displacement, as in the sense of giving to a contracting party more than an equitable share for the subsidizing product, to make a subsidy challengeable; however, the *SCM Agreement* did. This means that the *SCM Agreement* raised the standards for challengeability for subsidization of agricultural products that has impact on exports. Actually, because the TRSC had already associated the concepts of displacement and equitable share, it was not even a new provision. The *SCM Agreement* made clearer what the TRSC had already established.

It could be argued that *SCM Agreement* Art. 6.3(d) only requires for challengeability an increase in the world market share in a particular subsidized primary product. There is no requirement of displacement. However, if the increase in the share does not displace exports of another Member, this subsidy will not be challenged. Therefore, even though *SCM Agreement*

Art. 6.3(d) does not mention displacement, it has to occur in a possible challenge; otherwise, there is no interest in challengeability.

The *SCM Agreement* made clearer the concept that displacement is needed to challenge a subsidy that artificially increases the market share of a Member. It could be stated that displacement was implicit in the *GATT 1947* concept of “more than an equitable share,” but it was not. In *France – Wheat Exports*, the panel concluded that French subsidies resulted in France’s having more than equitable share of world export trade, particularly in wheat flour.⁵⁸² This decision, as well as others covered in the first part of this study, did not analyze displacement to condemn agricultural subsidization.

Besides, there is no further elaboration in the *SCM Agreement* on the concept of displacement in comparison with the definition in the TRSC. As has been seen, there was a discussion during the *GATT 1947* years on whether displacement meant the world export trade in a particular product or trade in the product in an individual market. There is no clarification on this matter in the *SCM Agreement*.

The *SCM Agreement* also regulates countervailing measures. It considerably increased this discipline compared with the TRSC provisions, which meant more provisions and a higher level of complexity for challengeability. *SCM Agreement* Art. 10 was similar to TRSC Art. 1. Both articles established that Members should take all needed steps to apply countervailing duties according to the provisions of Art. VI of *GATT 1994* and its terms. The *SCM Agreement* added a statement that duties only could be imposed after the beginning of an investigation and, more importantly, defined that countervailing duties should be implemented according to the provisions of the *AoA*. This article is proof of the influence of the *GATT 1947* provisions that set up the framework, followed by the TRSC and the *SCM Agreement*. It also determines that *SCM*

⁵⁸² *France – Wheat Exports supra* note 64 at para. 9/18

Agreement provisions will be cumulatively applied with the *AoA* to regulate agricultural subsidies.

The next section will analyze *SCM Agreement* Part V relating to countervailing duties to further identify the concept of injury that was highly relevant for the challengeability of agricultural subsidies after the Uruguay Round. The concept of injury in *SCM Agreement* Art. 15 is the same as in that in Art 5 (a) of the *SCM Agreement*, which regulates actionable subsidies.⁵⁸³

II.5.5 Countervailing Duties and the *SCM Agreement*'s Concept of Injury

Prior to the analysis, it should be mentioned that, as was stated previously, countervailing duties are domestic measures to be applied in the national market of the importer, which is different from the conclusions to other challenges under the WTO dispute settlement system. The *SCM Agreement* divided the regulation of countervailing duties in application of Art. VI of *GATT 1994* into initiation and subsequent investigation, evidence, consultations, calculation of the amount of a subsidy, determination of injury, definition of domestic industry, provisional measures, undertakings, imposition and collection, retroactivity, duration and review, public notice and judicial review.

This section will not focus on the descriptive and comparative analysis of all of the provisions,⁵⁸⁴ but it is important to mention that the definition of injury in the TRSC included several market effect factors, and the *SCM Agreement* copied the paragraphs that defined subsidies from the TRSC. *SCM Agreement* Art. 15.1 defined the meaning of the word “injury” in *GATT 1994* Art. 6 by using market-effect parameters and in the exact same words as those used

⁵⁸³ See *SCM Agreement* n. 11.

⁵⁸⁴ See Annex II for a more detailed study of *SCM Agreement* provisions regulating countervailing measures.

in the TRSC. It was necessary to have an objective examination of several market effect factors.⁵⁸⁵ It should be noted that the concept of injury for countervailing duties is the same in *SCM Agreement* Part V.

Also, it should be noted that *SCM Agreement* Art. 15.2 established that none of these factors could give precise guidance to the determination of injury.⁵⁸⁶ In the TRSC, there was no clear and complete concept of an injury. Therefore, regarding substantive provisions, the *SCM Agreement* did not evolve much from the TRSC, not even regarding the concept of an injury.

SCM Agreement Art. 15.4 replicated the provision in TRSC paragraph 3, which established that an evaluation of the impact on the domestic industry shall take into account an evaluation of “all” relevant economic factors that interfered in the state of the importing country’s industry that might be harmed by subsidies of the exporting country.⁵⁸⁷ The *SCM Agreement* followed the complex set of economic factors described in the TRSC to determine injury. However, the same Art. 15.4 states that none of these economic factors would give decisive guidance for the determination of an injury. Thus, the *SCM Agreement* kept the same general concept of an injury that it had inherited from the TRSC.

The *SCM Agreement* determines that the causal relationship between injury and subsidization must be determined by all relevant evidence. Investigating authorities must also examine other factors other than subsidized imports that are injuring the domestic industry. For this reason, it is important to know the volume and prices of the non-subsidized imports, as well

⁵⁸⁵ See *SCM Agreement* Art. 15.1 and TRSC Art 6.1 and 6.2.

⁵⁸⁶ *Ibid.* at 15.2.

⁵⁸⁷ *SCM Agreement* Art. 15.4 established some economic factors that can influence in an injury determination. It is stated that the list is not exhaustive and no one of these several factors can give decisive guidance.

[A]ctual and potential decline in output, sales, market share, profits, productivity, return on investments, or utilization of capacity; factors affecting domestic prices; actual and potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investment and, in the case of agriculture, whether there has been an increased burden on Government support programmes.

as other factors.⁵⁸⁸ This list helps the investigating authorities determine the factors that can interfere in the causal link between subsidy and injury. However, determining how much a factor, such as development in technology, influences the price of an exported product being investigated is a highly complex procedure. There is one paragraph in the article that says that one isolated factor cannot give decisive guidance, but the total of the factors considered must lead to a conclusion that protective action is necessary in order to avoid future material injury. This paragraph states that determining injury is complex, and a threat of it is even more difficult; however, if these factors are combined, they can give an indication as to the threat of injury.

The influence of the TRSC was significant after the Uruguay Round through the implementation of the *SCM Agreement*, which followed not only the structure of the TRSC but also adopted several of its provisions.

II.6 Conclusion

It has been shown that, during the Uruguay Round, the trade-distortive measures were replaced by numeric commitments. For export subsidies, a reduction of 36% of outlays and 21% reduction of subsidized exports was required. Regarding domestic support, developed countries had to reduce total AMS by 20%, with the exception of green and blue box measures.⁵⁸⁹

An examination of the numbers seems to show that the Uruguay Round succeeded in reducing trade-distortive measures. However, this conclusion does not survive a deeper analysis. First, tariffs on agriculture are still much higher when compared with those on industrial goods. Second, through the process of tariffication, tariffs were bound at a higher level than the majority

⁵⁸⁸ See *SCM Agreement* Art. 15.5.

⁵⁸⁹ The number for developing countries were the following: 24% of reduction 10% (per tariff line) on market access; 24% of reduction on outlays on export subsidies and 14% of reduction in subsidized exports and 13.3% of reduction on domestic support measures. Josling, "Forward Looking Assessment" *supra* note 342 at 3.

that existed prior to application of the Uruguay Round. Besides, the *AoA* negotiations are not yet concluded, and an agreement on modalities has not yet been agreed upon, which means that the numeric goals described above have not even been completely implemented.

Export subsidies have not been banned and remain a major distortion of trade in agriculture. On domestic support, the allocation of subsidies that were not really “green” in the green box measures is another current problem. Other flaws included the EU compensation payments and the US deficiency payments (blue box measures), which were exempt from the reduction commitments, to quote only some examples discussed above in this chapter.

The Uruguay Round agreements were also conceived of to solve problems with the inaccuracy of previous *GATT 1994* provisions, such as “more than an equitable share.” It seems, however, that the more elaborate regulations of the *AoA* and *SCM Agreement* also included new concepts that needed the help of the Appellate Body to be interpreted and limited. *Korea – Commercial Vessels* showed that concepts like adverse effects, serious prejudice and price suppression/depression are not crystal clear.

This is not to say that the WTO agreements were completely flawed in regards to the liberalization of agricultural trade. However, the result is far from the objectives stated in the preamble of the *Agreement on Agriculture*: to establish a fair and market-oriented agricultural trading system.

II.6.1 Challengeability of Agricultural Subsidies under the Uruguay Round Before the Expiry of the Peace Clause

The shield of the Peace Clause established by the Uruguay Round’s framework was a step back in regards to challengeability on agricultural subsidies. This conclusion is reached by

comparing the table for challengeability during the GATT years in the conclusion of the first part of this study and the table below. Under the *GATT 1947*, it was possible to challenge export subsidies if they had given a Member more than an equitable share of the market for the subsidized product.

The more elaborate framework of the WTO made the challengeability of agricultural subsidies almost impossible during the peace period, as the diagram below shows. It was not possible to challenge green box subsidies on any legal ground. Non-green box subsidies could be challengeable only if they were higher than 1992 levels, and even export subsidies could not be actionable if there was no injury.

Table 5: Challengeability of Agricultural Subsidies During the Peace Years

Boxes	CVDs (<i>GATT 1994</i> Art VI)	<i>SCM Agreement</i> Art 5 & 6	<i>GATT 1994</i> Art XVI	NV N or I (<i>GATT 1994</i> Art. II and XXIII 1(b))
Green (<i>AoA</i> Annex II)	No	No	No	No
Non-Green (<i>AoA</i> Art 6)	No, if there is no threat or injury	No, subsidies < 1992 levels	No, subsidies < 1992 levels	No, subsidies < 1992 levels
Export	No, if there is no threat or injury	No	No	No ⁵⁹⁰

⁵⁹⁰ The Peace Clause did not expressly hinder the challengeability of export subsidies under *GATT* Art. XXIII possibly because the Article does not expressly mention export subsidies. However, the Peace Clause explicitly hindered the challengeability of export subsidies under *GATT* Art. XVI. Since export subsidies were prohibited under *GATT* Art. XVI during the peace years, the likelihood of a successful challenge to these subsidies under *GATT* Art. XXIII was nil.

It is clear that the conclusion of the agreements that regulated agricultural trade after the WTO were not accompanied by significant liberalization. The steps required for challengeability were some of the main reasons for this.

CHAPTER III

THE LEGAL REGIME FOR AGRICULTURAL SUBSIDIES AFTER THE EXPIRY OF THE PEACE CLAUSE

Since the Uruguay Round, the agricultural sector has still been significantly distorted by subsidies and tariff policies. Agriculture was a major point of disagreement that contributed to the Doha Round's deadlock, partly because the Uruguay Round did not succeed in limiting WTO Members' abilities to subsidize domestic agricultural production, as illustrated in the second part of this study.⁵⁹¹

III.1 An Overview of Agriculture after the Uruguay Round

The *AoA* did not succeed in limiting or impeding agricultural subsidization practices. There are estimates that, if the Doha Round results in the lowering of trade barriers by 50%, this would represent a significant long-term global benefit.⁵⁹² Sixty-five percent of the benefits of this possible liberalization would go to the agriculture and food sectors.⁵⁹³

According to the WTO's data, in 1995 (the year the Uruguay Round agreements went into effect), most WTO Members guilty of the heaviest subsidization were far below their

⁵⁹¹ Josling observed that ceilings on domestic support agreed to as part of the *Agreement on Agriculture* do not function as a restraint on the largest subsidizing WTO Members, including the US, Japan or the EC. Josling, "Forward Looking Assessment" *supra* note 342 at 159-60.

⁵⁹² This is an Anderson's estimation based on World Bank data. See note *below*.

⁵⁹³ Anderson states that 64.8% of contributions to global economic welfare gains from removing trade barriers would come from the agriculture and food sector. Kym Anderson, "Agricultural Trade reform and poverty reduction in developing countries" *World Bank Policy Research Working Paper 3396, 2004* (Washington D.C.: WB-DRG-TT, 2004) at table 1.

permitted AMS ceilings. The US was using only 26.9% of its permitted AMS, the EC, 63.6%, Japan, 73.1%, Mexico, 4.8% and Canada 15%.⁵⁹⁴

The World Bank predicts that removing trade barriers in agriculture could raise hundreds of millions of people out of poverty. There is estimation that removal of trade barriers in agriculture by industrial countries could reduce poverty worldwide by 8%, or for about 200 million people.⁵⁹⁵ Some countries with lower labour costs tend to have a comparative advantage in agricultural production, because they are likely to export products with less aggregated value. This is why agricultural products constitute a significant percentage of the GDP of these countries.

As an example, the agricultural sector accounts for 29% of GDP and employs approximately 314 million people in India.⁵⁹⁶ Although countries with lower labour costs tend to have trade deficits in food and agriculture, they often have even greater deficits in non-food imports and, therefore, may gain from trade liberalization, so long as they have a comparative advantage in food.⁵⁹⁷ With the exception of Bangladesh, “countries with a comparative disadvantage in food account for only 29 percent of the total number of poor people.”⁵⁹⁸

These figures have been presented because the key objective of the Doha⁵⁹⁹ negotiations is to remove trade barriers to agriculture. Moreover, liberalizing agricultural trade may bestow even greater advantages on countries that subsidize than on countries⁶⁰⁰ that do not. According

⁵⁹⁴ *Ibid.* at Table 7.1

⁵⁹⁵ Cline, *Trade Policy supra* note 11 at 150.

⁵⁹⁶ Asoke Mukerji, “Developing Countries and the WTO: Issues of Implementation” (2000) 34 *Journal of World Trade* 33 at 39–40.

⁵⁹⁷ Cline, *Trade Policy supra* note 585 at 134.

⁵⁹⁸ *Ibid.* at 134–35.

⁵⁹⁹ *Doha Ministerial Declaration supra* note 445 at para. 13.

⁶⁰⁰ Anderson showed that estimated welfare gains to developed countries resulting from completely removing trade barriers in the agriculture sector would exceed gains to developing countries. Anderson, Kym. “The Challenge of Reducing Subsidies and Trade Barriers” *World Bank Policy Research Working Paper 3415, 2004* (Adelaide: WBG-ITU and CEPR, 2004) at table 2 [Anderson, “Reducing Subsidies”].

to Cline, because subsidies have a depressing effect on prices, it seems that eliminating agricultural subsidies would benefit countries that do not subsidize. However, these countries would have to be net food importers in order to take advantage of low-priced agricultural subsidized products, and that does not happen frequently. Actually, some studies suggest that most of the world's countries with lower labour costs are net food-exporting countries.⁶⁰¹

Therefore, despite the more elaborate provisions of the *AoA* and *SCM Agreement*, the new legal framework for agricultural subsidies brought in by the Uruguay Round was not able to restrain high levels of agricultural subsidization. Neither the agreements of the Uruguay Round nor the ongoing agricultural negotiations under the Doha mandate were able to come to a full agreement on modalities.

This means that Members have not agreed on specific numbers to reduce subsidy levels, nor have they agreed on the length of the implementation period. Reduction coefficients for AMS⁶⁰² and overall trade-distorting domestic support have not been defined, and green box measures still have to be revised under a methodology to be determined. All these uncertainties mean that distortions remain.⁶⁰³

The next section will help to better identify the limits of the challengeability for agricultural subsidies after the expiry of the Peace Clause under the overlapping regulations of the *GATT 1994*, *SCM Agreement* and *AoA*.

⁶⁰¹ Cline, *Trade Policy supra* note 11 at 133-34.

⁶⁰² See *supra* note 386.

⁶⁰³ Mario de Queiros Monteiro Jales, "Domestic Support to Agriculture in Developing Countries" *Paper prepared for the FAO Workshop on WTO Rules for Agriculture Compatible with Development on Rome 2-3 February 2006* (Sao Paulo: ICONE, 2006) at 30.

III.2 Legal Principles of Interpretation and the Relationship among the *AoA*, *SCM Agreement* and *GATT 1994*

The *AoA* established the WTO as the regime for agricultural products, while the *GATT 1994* and the *SCM Agreement* purportedly apply to all goods, with some limitations for agricultural products. *AoA* Article 13 had limited the application of the *SCM Agreement* and *GATT 1994* to agricultural products. The expiration of the Peace Clause lifted the temporary restraint of challengeability for agricultural subsidization regulated by three different agreements. Therefore, it is of note to verify how leading principles of international law and leading principles of interpretation interact in the relationship among these Agreements after the expiry to determine the new limits on challengeability for agricultural subsidies.

III.2.1 Applicable Principles of International Law

Art. 38 of the Statute of the International Court of Justice defines the sources of international law:

1. The Court, whose function is to decide in accordance with international law such disputes as are submitted to it, shall apply: a. international conventions, whether general or particular, establishing rules expressly recognized by the contesting states; b. international custom, as evidence of a general practice accepted as law; c. the general principles of law recognized by civilized nations; d. subject to the provisions of Article 59, judicial decisions and the teachings of the most highly qualified publicists of the various nations, as subsidiary means for the determination of rules of law. 2. This provision shall not prejudice the power of the Court to decide a case *ex aequo et bono*, if the parties agree thereto.

According to the principles of international law, there is a fundamental rule for treaty interpretation. This rule has been expressed through Arts. 31 and 32 of the Vienna Convention, which established:

Article 31. General rule of interpretation

1. A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose.

2. The context for the purpose of the interpretation of a treaty shall comprise, in addition to the text, including its preamble and annexes: (a) any Agreement relating to the treaty which was made between all the parties in connexion with the conclusion of the treaty; (b) any instrument which was made by one or more parties in connexion with the conclusion of the treaty and accepted by the other parties as an instrument related to the treaty.

3. There shall be taken into account together with the context:

(a) any subsequent Agreement between the parties regarding the interpretation of the treaty or the application of its provisions; (b) any subsequent practice in the application of the treaty which establishes the Agreement of the parties regarding its interpretation; (c) any relevant rules of international law applicable in the relations between the parties.

4. A special meaning shall be given to a term if it is established that the parties so intended.

Article 32 Supplementary means of interpretation

Recourse may be had to supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion, in order to confirm the meaning resulting from the application of article 31, or to determine the meaning when the interpretation according to article 31: (a) leaves the meaning ambiguous or obscure; or (b) leads to a result which is manifestly absurd or unreasonable.⁶⁰⁴

One of the corollaries of the “general rule of interpretation” in the *Vienna Convention* is that interpretation must give meaning and effect to all the terms of a treaty. An interpreter is not free to adopt a reading that would result in reducing whole clauses or paragraphs of a treaty to redundancy.⁶⁰⁵

Arts. 31 and 32 of the Vienna Convention provide the foundation for the treaty-interpretive process. That is, “interpretation must be based above all upon the text of the treaty” and all other

⁶⁰⁴ *Vienna Convention on the Law of Treaties*, 23 May 1969, 1155 U.N.T.S. 331 at 12, (entered into force 27 January 1980) [*The Vienna Convention*].

⁶⁰⁵ Carreau, Dominique & Juillard, Patrick, *Droit International Economique* (Paris : Dalloz, 2003) at para. 369.

treaties, agreements or practices related to that treaty.⁶⁰⁶ The provisions of the treaty are to be attributed their usual meaning when used in their particular context. The object and purpose of the treaty are also to be taken into account in determining the meaning of its provisions. If, for example, there is a reference in one treaty or agreement to another treaty or agreement concluded at the same time among the parties or subsequently, according to the Vienna Convention, it must be considered in order to interpret the treaty properly.⁶⁰⁷

It should be noted that the rule of treaty interpretation established in Art. 31 of the Vienna Convention has achieved the status of a rule of customary international law, due to the amount of cases to which it has been applied.⁶⁰⁸ As such, it forms part of the "customary rules of interpretation of public international law." According to DSU Art. 3.2. the "[DSU] serves to preserve the rights and obligations of the Members under the covered agreements, and to clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law." This provision officially received the *Vienna Convention* as one of the sources of international law that must guide WTO principles and rules.

The conclusion is that both panels and the Appellate Body must be guided by the rules of treaty interpretation set out in the *Vienna Convention* that determine a set of factors that must be considered for the interpretation of a treaty, which means that it cannot be interpreted in isolation. This rationale was confirmed by some WTO panels and the Appellate Body. In *India – Patent Protection for Pharmaceutical and Agricultural Chemical Products [India – Patents (US)]*, the Appellate Body relied on the customary rules of interpretation of public international law as a basis

⁶⁰⁶ *Case Concerning Maritime Delimitation and Territorial Questions (Qatar v. Bahrain)*, Judgment of 16 March 2001 [2001] I.C.J. Rep. 40. [*Qatar v. Bahrain ICJ*]

⁶⁰⁷ Francisco J. Rezek. *Direito Internacional Publico: Curso Elementar*, 7th Ed. (Sao Paulo: Saraiva, 1998).

⁶⁰⁸ See *Golder v. United Kingdom*, (1995), 18 Eur. Ct. H.R. (Ser. A) 1 E.H.R.R. 524.

for the interpretative principle.⁶⁰⁹ Specifically the AB relied on Article 31 of the *Vienna Convention*, stating that the duty of a treaty interpreter is to examine the words of the treaty to determine the intentions of the parties.⁶¹⁰

The Appellate Body in the case *United States – Standards for Reformulated and Conventional Gasoline [United States – Gasoline]*⁶¹¹ has been directed, by Article 3(2) of the *DSU*, to apply to clarify the provisions of the *GATT 1994* and the other "covered agreements" of the "Marrakesh Agreement Establishing the World Trade Organization."⁶¹² This directive reflects a measure of recognition that neither *GATT 1994* nor any other WTO agreement is to be read in isolation.

Vienna Convention Art. 31, paragraph 2 establishes that the context for the interpretation of a treaty must take into account: (a) "any Agreement related to the treaty which was made between all the parties in connexion with the conclusion of the treaty". If any agreement has to be considered for the interpretation of the treaty, agreement or provision – especially if they have some aspects of common regulation – the *SCM Agreement*, the *AoA* and the *GATT 1994* can be applied together, especially to regulate the challengeability of agricultural subsidies where there are mentions of cross regulation between the three Agreements.

The Vienna Convention establishes some principles for treaty interpretation in Arts. 31 and 32, which were accepted and applied by the WTO through *DSU* Art. 3(2). Therefore, under the Vienna Convention Art. 31, especially paragraphs 2 and 3, the *AoA*, the *SCM Agreement* and the

⁶⁰⁹ See also *Case Concerning Territorial Dispute (Libyan Arab Jamahiriya v. Chad)*, Judgment of 3 February 1994 [1994] I.C.J. Rep. 6 and *Qatar v. Bahrain ICJ supra* note 605.

⁶¹⁰ In *India – Patent* it was observed that "[t]he Appellate Body has recognized that both Article 31 and Article 32 of the Vienna Convention apply to disputes under the WTO Agreement. Appellate Body Report, *India – Patent Protection for Pharmaceutical and Agricultural Chemical Products* (1998), WTO Doc. WT/DS50/AB/R, adopted 16 January 1998, DSR 1998:I, 9 at n. 40 [*India – Patents (US)*] See also Appellate Body Report, *Japan – Taxes on Alcoholic Beverages* (1996), WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, DSR 1996:I, 97 at 105 [*Japan – Alcoholic Beverages II*].

⁶¹¹ *US – Gasoline supra* note 8 at 17.

⁶¹² *The Marrakesh Declaration supra* note 286.

GATT 1994 cannot be interpreted in isolation to regulate the challengeability of agricultural subsidies.

The next section will examine which WTO principles also corroborate the standards of interpretation established by the “cohesion of treaties” and the Vienna Convention.

III.2.2 Applicable Principles of the World Trading System

WTO provisions and panels have already established some principles on the interpretation of and relationship among its agreements, which include the *GATT 1994*, the *SCM Agreement* and the *AoA*. According to Didier Chambovey, there are two principles that control the relationship between WTO Annex I⁶¹³ Agreements. The first is the cumulative principle that states that all WTO Annex I Agreements are integral parts of the same treaty, the WTO Agreement.⁶¹⁴ All the provisions of these Agreements should be read as “an inseparable package of rights and disciplines which have to be considered in conjunction.”⁶¹⁵ In this case, Annex I Agreements would normally apply cumulatively, except if there were a conflict. Chambovey observes that the Appellate Body, however, has already made it clear that “two articles dealing with the same aspect of the same case in point could apply cumulatively even if there are distinctions between the drafting of the two provisions.”⁶¹⁶

The second rule of interpretation, according to Chambovey, is the principle of effective interpretation, *l'effect utile* in French and *ut res magis valeat quam pereat* in Latin. According to

⁶¹³ Annex 1A of Marrakesh Agreement Establishing the World Trade Organization comprises all the Multilateral Agreements on Trade and Goods. *WTO Legal Texts supra* note 1 at vi.

⁶¹⁴ *The Marrakesh Agreement supra* note 286.

⁶¹⁵ Appellate Body Report, *Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items* (1998), WTO Doc. WT/DS121/AB/R at para. 81 adopted 12 January 2000, DSR 2000:I, 515 [*Argentina – Footwear (EC)*].

⁶¹⁶ Chambovey “Peace Clause” *supra* note 9 at n. 16.

him, this principle, which has been applied many times by WTO panels and the Appellate Body⁶¹⁷ – means that an interpreter cannot choose an interpretation “that would result in reducing whole clauses or paragraphs of a treaty to redundancy or inutility.” He states that this theory was confirmed by the Appellate Body, referring to the relationship between *GATT 1994* Art. XIX and the Agreement on Safeguards⁶¹⁸ which decided that WTO agreements were an inseparable package of rights and disciplines must, accordingly, “be one that gives meaning to all the relevant provisions of these two equally binding Agreements.”⁶¹⁹

Chambovey presents the rationale that, according to the principle of effective interpretation, the *SCM Agreement* would not apply to agricultural subsidies. *AoA* Art. 21.1 states that “the provisions of the *GATT 1994* and of other Multilateral Trade Agreements in Annex 1A to the WTO Agreement shall apply subject to the provisions of this Agreement.” *EC – Bananas*⁶²⁰ set the precedent that provisions of *GATT 1994* and Annex 1A Agreements applied to agricultural products “except to the extent that *AoA* contained specific provisions dealing specifically with the same matter.”⁶²¹

According to Chambovey, the principle established in *EC – Bananas* that the *SCM Agreement* cannot be applied to agricultural subsidies has been wrongly applied by the international community. In his view, the *AoA* contains “specific provisions dealing specifically with the same matter” as the *SCM Agreement* on domestic and export subsidies and, for this reason, according to *EC – Bananas*, the *SCM Agreement* does not apply to agricultural subsidies.

⁶¹⁷ *Ibid.* at n.17.

⁶¹⁸ *Agreement on Safeguards. WTO Legal Texts supra* note 1.

⁶¹⁹ The statement its origins in the Vienna Convention Art. 31. *Vienna Convention supra* note 604.

⁶²⁰ Appellate Body Report, *European Communities – Regime for the Importation, Sale and Distribution of Bananas* (1997), WT/DS27/AB/R, adopted 25 September 1997, DSR 1997:II, 591 [*EC – Bananas III*].

⁶²¹ *Ibid.* at para. 155.

Chambovey goes further to state that *AoA* and *SCM Agreement* have very different natures. The first establishes quantitative limits for agricultural subsidies and the second defines in qualitative terms situations where subsidies are completely prohibited or actionable. He states that the *AoA* was tailored to create a distinct regime for agricultural subsidies, and the general rules of the *SCM Agreement* are not suited for the idiosyncratic conditions of agriculture.

He also states that, if the *SCM Agreement* applied to agricultural subsidies, agricultural subsidies would have a more rigorous regime than would non-agricultural subsidies, which would go against the history of the Uruguay Round negotiations, which aimed at creating a less rigorous regime.⁶²² He recognizes however that *AoA* Art. 21.1⁶²³ aims at establishing a less distortive regime for agriculture. According to him, agricultural subsidies should be regulated in the same way as non-agricultural subsidies at the end of the reform process. According to him, the end of the reform process did not occur when the Peace Clause expired in December 31, 2003, and for this reason, agriculture still has to be treated separately. However, he did not specify when the reform process would finish. Chambovey concluded by stating that if WTO negotiators wanted to make agricultural subsidies challengeable under the *SCM Agreement*, there would be a provision in one of the agreements that would expressly state so..

Regarding the Peace Clause, the author states that its mere existence proves that the *SCM Agreement* was not meant to apply to agriculture, because the expiry of the Peace Clause does not make the *SCM Agreement* immediately applicable to agricultural subsidies. In this way, agricultural subsidies would lose their *a priori* protection against actions from the *SCM Agreement* and *GATT 1994*. Chambovey states that the *AoA* would supersede other Annex 1A

⁶²² Appellate Body Report, *European Communities—Measures concerning Meat and Meat Products (Hormones)* (1996), WTO Doc. WT/DS26/AB/R, WT/DS48/AB/R, at para. 165 adopted 13 February 1998, DSR 1998:I, 135 [*EC – Hormones*].

⁶²³ *AoA* Art. 21.1 states that “[t]he provisions of GATT 1994 and of other Multilateral Trade Agreements in Annex 1A to the WTO Agreement shall apply subject to the provisions of this Agreement”.

agreements in two overlapping situations. The first is that of a conflict between provisions dealing with the same matter, and the second is when a provision of another Annex 1A agreement does not enable the AoA to have appropriate effects, though the author does not explain the meaning of “appropriate effects.”⁶²⁴

Richard Steinberg and Timothy Josling disagree with Didier Chambovey. In their article on the Peace Clause⁶²⁵ they state that the *GATT 1994*, *SCM Agreement* and *AoA* have to apply cumulatively to create a coherent system to regulate agricultural subsidies. This view would be in accordance with panel and AB decisions.⁶²⁶ According to them, two principles could govern the cumulative application of the WTO agreements. The first one would be that in case of conflict the most specific agreement would prevail⁶²⁷ and the second would be the public international law principle of effective interpretation, the same quoted by Chambovey, which states that agreements have to be interpreted to give meaning and legal effect to all the terms.⁶²⁸

For Steinberg and Josling this principle states that WTO Annex1A Agreements have to be interpreted consistently with each other, which means that they have to be applied together for regulation of agricultural subsidies. According to Chambovey, this principle means that the *SCM Agreement* cannot be applied to agricultural subsidies, because there is a conflict between the *SCM Agreement* and *AoA* that hinder common applicability for agricultural subsidies and gives precedence to the *AoA*.

The explanation for the difference in interpretation of the same principle lies in the concept of conflict. The next section of this study will demonstrate that there is no conflict among the *GATT 1994*, the *SCM Agreement* and the *AoA* regarding the regulation of agricultural

⁶²⁴ Chambovey “Peace Clause” *supra* note 9 at 313.

⁶²⁵ Steinberg, “Peace Clause” *supra* note 7 at 1.

⁶²⁶ *Ibid.* at n. 20, 21 and 22.

⁶²⁷ *Ibid.* at n 23.

⁶²⁸ *Ibid.* at n 24.

subsidies. The international trading system always tries to find a way to avoid conflicts among the agreements, as demonstrated in *Indonesia – Autos* through the public international law presumption against conflicts among international agreements.⁶²⁹

According to the panel in *Brazil – Desiccated Coconut*⁶³⁰ international trade encompasses the *GATT 1994*, the results of past trade liberalization efforts and all of the results of the Uruguay Round of Multilateral Trade Negotiations. This means that all WTO agreements must be read as a set that cannot be separated.

Article II.2 of the *Marrakesh Agreement*,⁶³¹ which established the WTO, states that multilateral trade agreements are “integral parts” of the WTO Agreement, “binding on all Members.” This⁶³² is reflected in several articles of the WTO Agreement articles, including those on accession, non-application, acceptance and withdrawal. The DSU also established that the integrated framework of dispute settlement had to be applied to “all covered agreements.”

In *Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items* [*Argentina – Footwear (EC)*],⁶³³ the Appellate Body Report, with respect to the relation between the Agreement on Safeguards and the *GATT 1994*, determined that the panel was correct to rule that “Article XIX of *GATT 1994* and the Safeguards Agreement must be read as an “inseparable package of rights and regulations”, which has to be considered as a whole.⁶³⁴ This statement confirmed the decision in *Brazil – Desiccated Coconut* on the unity of all WTO

⁶²⁹ *Ibid.* at 6.

⁶³⁰ *Brazil – Desiccated Coconut* *supra* note 187 at 10-12.

⁶³¹ *The Marrakesh Agreement* *supra* note 286 at Art. II 2.

⁶³² The “Single Undertaking” was established in paragraph 47 of the *Doha Ministerial Declaration* *supra* note 447. It is one of the most relevant WTO principles and states that: “[v]irtually every item of the negotiation is part of a whole and indivisible package and cannot be agreed separately. ‘Nothing is agreed until everything is agreed.’” online: WTO http://www.wto.org/english/tratop_e/dda_e/work_organ_e.htm

⁶³³ *Argentina – Footwear (EC)* *supra* note 614 at paras. 79-81.

⁶³⁴ *Ibid.* at 25.

agreements for interpretation purposes. One agreement cannot be read in isolation from the others.

Moreover, according to the Appellate Body report, the treaty interpreter must read all applicable provisions of a treaty in a way that gives meaning to all harmoniously.⁶³⁵ This confirms that WTO agreements have to be interpreted as an "inseparable package of rights and regulations" as quoted in the WTO case above, giving meaning to all relevant provisions of their equally binding agreements.

Chambovey stated that the *SCM Agreement* could not be applied to regulate agricultural subsidies, because he mistakenly found that there was a conflict between the *SCM Agreement* and the *AoA*, as will be seen in the next section. On the other hand, Steinberg and Josling stated that both Agreements could be applied together, because *AoA* Art. 21.1 states that "*GATT 1994* ... and other Multilateral Trade Agreements in Annex 1A to the WTO Agreement shall apply subject to the provisions of this Agreement," which suggests that the *AoA* was not meant to be applied exclusively.⁶³⁶

There is no flaw in Josling and Steinberg's conclusion, but their premises that led to such a conclusion were mistaken. The *AoA* and *SCM Agreement* must be interpreted together regarding the challengeability of agricultural subsidies, but the principle of effective interpretation alone does not give the concrete legal base to such conclusion. The reason is that, if there were a conflict between the *SCM Agreement* and the *AoA*, the latter would prevail over the former, and agricultural subsidies could not be challenged under the *SCM Agreement*. This is why the General Interpretative Note to Annex 1A establishes that, if there is a conflict between

⁶³⁵ *US – Gasoline supra* note 8 at 23; *Japan – Alcoholic Beverages II supra* note 609 at 12 and *India – Patents (US) supra* note 609 at para. 45.

⁶³⁶ Steinberg, "Peace Clause" *supra* note 7 at n. 28.

the *GATT 1994* and any provision of any Annex 1A agreement, the provision of the Agreement shall prevail over the *GATT 1994* throughout the extent of the conflict.⁶³⁷

The principles of international law; principles of international trading law; *AoA* Art. 21.1; the cross-references among *AoA*, *SCM Agreement* and *GATT 1994*; and the WTO panel and AB decisions indicate these three Agreements must be interpreted together. However, there is no possibility of more than one agreement regulating the same subject if there is a conflict among them. In this case, the most specific agreement must apply.

For example, *AoA* Art. 21.1 states that all WTO agreements have to be considered as part of a package to regulate trade, but it does not state that “in case of conflict *GATT 1994* ... and other Multilateral Trade Agreements in Annex 1A to the WTO Agreement shall apply.” The principle in international law of the “cohesion of treaties” or the world trading principle of a single undertaking state that each agreement is part of a bigger and more complete system. Therefore, the interpreters must find a way to take into account the whole package when an agreement is read. Several decisions quoted in this section have corroborated this view, which has its origin in Art. 31 of the Vienna Convention, which has attained the status of customary international law and been internalized in the trading system through DSU Art. 3.2. Therefore, the key point that must be analyzed for a verification of challengeability upon expiry of the Peace Clause is the concept of conflict, which will be analyzed next.

III.2.3 Conflict among Agreements

For the purposes of this study, whether there is a conflict among the agreements that regulate agricultural subsidies should be examined. This study used two methodologies to look at

⁶³⁷ *WTO Legal Texts supra* note 1 at 16.

the pertinent legislation. The first was theoretical, because it was based on a doctrine that developed some requirements or thresholds to identify conflict among WTO agreements. The second was the same methodology applied by the WTO to resolve conflicts among WTO agreements.

These two methods were chosen because there is a need to examine three WTO agreements and, more specifically, whether there is conflict among them. The reason to apply these two methods is that the first one is theoretical and the second one is empirical. A normative analysis of the *AoA*, *SCM Agreement* and *GATT 1994* could have not only a theoretical examination of conflict, but it could also include the empirical method that was already used by the WTO to resolve conflicts among WTO agreements. There is a WTO rationale to resolve conflicts among its agreements that has to be considered as well as theoretical research by scholars who study the WTO and help to shape the system. If the normative analysis results in one conclusion when the empirical method is being applied and a different conclusion when the theoretical method is applied, there is a higher probability of this conclusion being wrong. Conversely, if the conclusion is the same with the use of both methods, there is a higher probability of this conclusion being right.

The broader concept of the word “empirical,” adopted from Lee Epstein and Gary King, is used in this study.⁶³⁸ According to their definition, this word has come to take on a particularly narrow meaning—one associated purely with statistical techniques and analyses, or quantitative data. However, they prefer a broader concept: evidence of the world based on experience and

⁶³⁸ “[E]mpirical – that is, learning about the world using quantitative data or qualitative information ... basing conclusions on observation or experimentation—and *inference* ... using facts we know to learn about facts we do not know” Epstein, Lee & King, Gary. “The rules of Inference” (2002) 69 *The University of Chicago Law Review* 1 at 1-2.

observation.⁶³⁹ According to them, what defines whether a research is empirical is the data that can be “facts based on legislation,” “case law” or the “outcomes of secondary archival research or primary data.” In other words, data can be legal and “as long as research involves data that is observed, or desired, it is empirical.”⁶⁴⁰

This research not only analyzed the wording of the three agreements (normative analysis) under a theoretical method, but also took into account WTO decisions in the belief that not only the concept of conflict reached by scholars but also how the panelists and the AB have decided is relevant. And in this sense, the second method (examination of WTO decisions) is empirical, because it involves “legal data that is observed.”

This examination is primarily qualitative (non-numerical). The goal of this study is to analyze substantive provisions of three specific WTO agreements to reach a specific conclusion. This analysis does not involve numbers, but the analysis of substantive provisions of three agreements to apply the theoretical and empirical concepts of conflict.

III.2.3.1 The Theoretical Methodology to Identify Conflict

There are several authors who approach or conduct research on the conflict among laws. However, most of the publications only refer to national law. A few authors have written about the conflicts in public international law; however, most of these authors have not written about

⁶³⁹ “[W]hen I speak of empirical legal scholarship I refer only to the subset of empirical legal scholarship that uses statistical techniques and analyses. By statistical techniques and analyses I mean studies that employ data (including systematically coded judicial opinions) that facilitate descriptions of or inferences to a larger sample or population as well as replication by other scholars.” Heise, Michael. “The Importance of Being Empirical” (1999) 26 *Pepperdine L Rev.* 810 in *Ibid* at n. 2.

⁶⁴⁰ *Ibid.* at 3.

the conflict between laws or norms or, specifically, about conflict among WTO agreements. This was the first reason that Joost Pauwelyn's methodology was chosen.

The second reason was that the methodology developed by Pauwelyn to identify conflict can also be applied to WTO agreements that are part of the same treaty.⁶⁴¹ The third reason is that his theory on finding conflict is unbiased, which means that it can be applied in other situations. It can be applied not only to identify conflict among the *AoA*, *SCM Agreement* and *GATT 1994* regarding the challengeability of agricultural subsidies, but also to identify conflict in any norm of international public law. According to Lee Esptein and Gary King, an unbiased measurement procedure tends to be more valid than a non-unbiased model.⁶⁴²

According to Pauwelyn⁶⁴³ the priority rules to resolve a conflict in applicable law are determined by three basic principles. The first is the contractual freedom of states, the second is *pacta sunt servanda*⁶⁴⁴ and the last is the principle *pacta tertiis nec nocent nec prosunt*.⁶⁴⁵

The first principle means that the latest expression of the state's intention shall prevail. The second principle, found in Vienna Convention Art. 26, says that every treaty is binding upon the parties that signed it. The third is from Art. 34 of the Vienna Convention, which states that a treaty does not create an obligation for a third state without its consent. Even though these principles can provide some guidance on the applicable law, they cannot provide a specific

⁶⁴¹ It is relevant to note that the *AoA*, *SCM Agreement* and *GATT* are three different Agreements from the same treaty. The concept of conflict in this research applies to different "norms" that comprise different treaties, Agreements or different provisions of the same treaty. This is the same concept applied by the WTO cases when they analyze conflict among different Agreements or different provisions of different Agreements. It is not included in the concept of "norm" pre-normative rules (drafts, *travaux préparatoires*, written intentions).

⁶⁴² *Supra* note 637 at 89-92.

⁶⁴³ Joost Pauwelyn, *Conflict of Norms in Public International Law: How WTO Law Relates to other Rules of International Law*, (Cambridge: Cambridge University Press, 2003) at 328. The analysis by Pauwelyn was used for the qualitative examination of WTO legislation. Pauwelyn is a former WTO legal affairs officer and author of a book on the conflict of laws in the WTO, which is one of the few books on the subject of conflict among WTO agreements and a leading source of information about the conflict of norms in international trading law.

⁶⁴⁴ *Vienna Convention* Art. 26 establishes that "[e]very treaty in force is binding upon th parties to it and must be performed by them in good faith". *Vienna Convention supra* note 604 cited in *Ibid.* at n. 1.

⁶⁴⁵ It is the same principle applied in the *Vienna Convention* Art. 34 that states "[a] treaty does not create either obligations or rights for a third state without its consent". *Vienna Convention supra* note 604 cited in *Ibid.* at n. 2.

solution to a possible conflict among the *GATT 1994*, *SCM Agreement* and *AoA*. These three Agreements are part of the same trading system and have the same signatories. Therefore, a further analysis is needed in order to verify whether there is a conflict among these Agreements regarding the challengeability of agricultural subsidies.

According to Pauwelyn's analysis, verification of whether the preconditions exist for a conflict in a specific case should take place. The preconditions are the overlapping of *ratione materiae, personae and temporis*⁶⁴⁶ meaning that agreements with potential conflict have to have some overlap in terms of the subject matter regulated, the parties that signed the agreements have to be the same and the agreements have to exist or interact at the same time. The *GATT 1994*, *SCM Agreement* and *AoA* fulfilled the three preconditions, which means that a conflict among them is possible.

It has been shown that the three WTO agreements to regulate agricultural subsidies contain the three preconditions for a conflict. Next, it is necessary to determine meaning of the term "conflict" and see if it can be found in the relationship among the *GATT 1994*, the *SCM Agreement* and the *AoA*.

Pauwelyn approaches the notion of conflict in a non-restrictive, non-dogmatic and open way according to his own definition. This means that he rejects the narrower and practical definition of other authors, who assume that there is a conflict among norms, treaties, agreements or provisions when there is a mutually exclusive obligation. He conceptualizes conflict as a normative inconsistency, incompatibility or contradiction that is opposed to norms that complement or confirm each other. The author continues and offers a clear definition:

⁶⁴⁶ *Ibid.* at 165.

“Essentially, two norms are, therefore in a relationship of conflict if one constitutes, has led to, or may lead to, a breach of the other.”⁶⁴⁷

To determine if compliance with one of the three Agreements regulating agricultural subsidies can lead to a breach of another, Pauwelyn divides norms of international law into four categories (command, prohibition, exemption and permission), according to the following table and diagram.

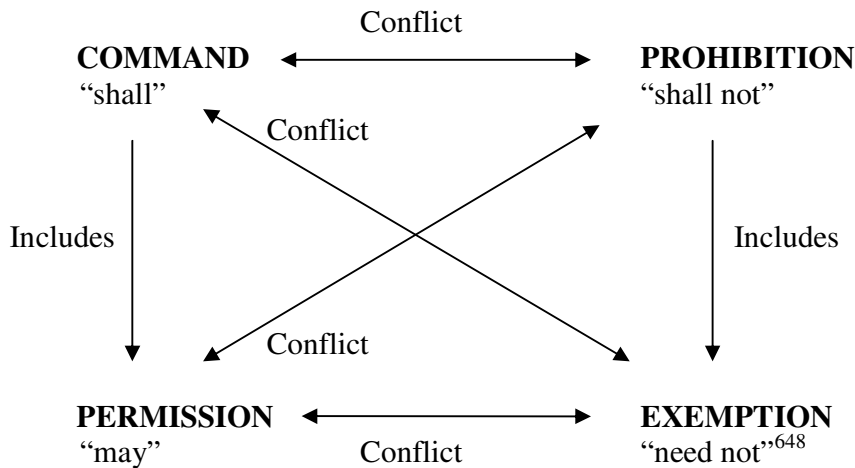
Frame 1: Theoretical Method – Four Types of Measures

Conflict Situation	Norm 1 (Obligation of state A vis-à-vis state B)	Norm 2 (Compliance with obligation, or exercise of right, by state A constituting a breach of Norm 1 vis-à-vis state B)
1	<i>Command:</i> in a given situation state A ‘ shall do ’ X	<i>Command:</i> in the same situation state A ‘ shall do ’ Y (Y being either different from or mutually exclusive with X)
2	<i>Command:</i> in a given situation state A ‘ shall do ’ X	<i>Prohibition:</i> in the same situation state A ‘ shall not do ’ X
3	<i>Command:</i> in a given situation state A ‘ shall do ’ X	<i>Right (exemption):</i> in the same situation state A ‘ need not do ’ X (it may, for example, do Y)
4	<i>Prohibition:</i> in a given situation state A ‘ shall not do ’ X	<i>Right (permission):</i> in the same situation state A ‘ may do ’ X

⁶⁴⁷ *Ibid.* at 176.

The four conflict situations are graphically described in the diagram below:

Diagram 1: Theoretical Method—Conflicts Between Norms



Now, we have the concept of conflict defined by Pauwelyn’s theoretical methodology. Before applying the test to the *GATT 1994*, *SCM Agreement* and *AoA*, we turn to empirical methodology to identify conflict according to its appearance in WTO cases.

III.2.3.2 The Empirical Methodology to Identify Conflict

The analysis of some WTO cases is qualitative, because not all WTO cases worked with the concept of conflict. Thus, the goal is to pick the passages of the WTO cases that defined or worked with the concept of conflict and apply this concept to the analysis of the three Agreements that are the objects of this study.

⁶⁴⁸ *Ibid.* at 179.

The definition of conflict among WTO Annex 1A Agreements has been addressed in some cases. In *Indonesia – Autos* quoting the Encyclopedia of Public International Law and the British Yearbook of International Law, the panel ruled:

...in international law for a conflict to exist between two treaties, three conditions have to be satisfied. First, the treaties concerned must have the same parties. Second, the treaties must cover the same substantive subject matter. Were it otherwise, there would be no possibility for conflict. Third, the provisions must conflict, in the sense that the provisions must impose *mutually exclusive obligations*. "... [T]echnically speaking, there is a conflict when two (or more) treaty instruments contain obligations which cannot be complied with simultaneously. ... Not every such divergence constitutes a conflict, however. ... Incompatibility of contents is an essential condition of conflict". (7 Encyclopedia of Public International Law (North-Holland 1984), page 468). The *lex specialis derogat legi generali* principle "which [is] inseparably linked with the question of conflict"(Idem., page 469) between two treaties or between two provisions (one arguably being more specific than the other), does not apply if the two treaties "... deal with the same subject from different point of view or [is] applicable in different circumstances, or one provision is more far-reaching than but not inconsistent with, those of the other" (Wilfred Jenks, "The Conflict of Law-Making Treaties", The British Yearbook of International Law (BYIL) 1953, at 425 *et seq.*).⁶⁴⁹

The effort to harmonize any possible conflict among agreements or provisions is clear in the panel's decision. As defined by the panel, the first threshold that a situation must reach in order to be defined as a conflict is that the provisions or agreements must include a) the same parties, b) the same substantive subject matter and c) a mutually exclusive obligation. In the third condition, equal obligations are not enough to characterize a conflict.

There must be incompatibility of the contents, and one treaty or provision must hinder the simultaneous compliance with another treaty or provision. The second threshold that a situation must reach to be defined as a conflict, as suggested by the panel, is that both treaties or provisions must deal with the same subject from the same point of view. This means that, even if

⁶⁴⁹ *Indonesia – Autos supra* note 234 at para 14.28.

the situation reaches the first threshold, it is not a conflict if the provisions or treaties are not written from the same point of view.

Trying to define what the panelist meant by the expression “same point of view” is not only beyond the scope of this study, but also inutile. The relevant aspect, evident from this decision, is that the interpreters must, in all circumstances, try to avoid conflict among provisions or treaties.

The Appellate Body brought in another condition to determine conflict in *Guatemala – Anti-Dumping Investigation Regarding Portland Cement from Mexico* [*Guatemala – Cement I*]. The Appellate Body, quoting the relationship between the special or additional dispute settlement provisions of the Anti-dumping Agreement and the Dispute Settlement Understanding (DSU), held that:

In our view, it is only where the provisions of the DSU and the special or additional rules and procedures of a covered Agreement *cannot* be read as *complementing* each other that the special or additional provisions are to *prevail*. A special or additional provision should only be found to *prevail* over a provision of the DSU in a situation where adherence to the one provision will lead to a violation of the other provision, that is, in the case of a *conflict* between them. An interpreter must, therefore, identify an *inconsistency* or a *difference* between a provision of the DSU and a special or additional provision of a covered Agreement *before* concluding that the latter *prevails* and that the provision of the DSU does not apply. We see the special or additional rules and procedures of a particular covered Agreement as fitting together with the generally applicable rules and procedures of the DSU to form a comprehensive, integrated dispute settlement system for the *WTO Agreement*. ... It is, therefore, only in the specific circumstance where a ... special or additional provision may be read to *prevail* over the provision of the DSU (more generic).”⁶⁵⁰

According to the panel in *Guatemala – Cement I*, the more specific treaty or provision prevails only if there is an inconsistency with the more generic one and if they cannot be read as

⁶⁵⁰ Appellate Body Report, *Guatemala – Anti-Dumping Investigation Regarding Portland Cement from Mexico*, (1998) WTO Doc. WT/DS60/AB/R at para 65 adopted 25 November 1998, DSR 1998:IX, 3767 [*Guatemala – Cement I*].

complementary to each other. The panel emphasized that both generic and specific provisions exist in order to form a comprehensive and integrated system.

This Appellate Body's interpretation is also consistent with the public international law presumption against conflicts. This is evident, especially when we analyze the other conditions for determining conflict found in *Indonesia – Autos*. It is also consistent with the WTO principle of "single undertaking."⁶⁵¹

It has been seen that there are three thresholds that must be reached for a situation to be characterized as a conflict. The first is that the three conditions in the provisions or agreements a) apply to the same parties, b) cover the same substantive subject matter, and c) contain mutually exclusive obligations. The second threshold can be reached on determining that the analyzed treaties or provisions deal with the same subject from the same point of view. The third and last threshold is reached when the more specific treaty or provision has an inconsistency when compared with the more generic one.

It could be stated that the thresholds and requirements of both methods are similar. The preconditions in the theoretical method are a) an overlapping of *rationae materiae, personae and temporis* b) the same parties having signed the agreements and c) the existence or interaction at the same time of the provisions of the agreements. The empirical method requires the verification of whether the agreements concern the same parties, substantive subject matter and mutually exclusive obligations.

The preconditions for the theoretical method are similar to those for empirical method, but the main requirements for the existence of a conflict (command, prohibition, permission and exemption) in the theoretical method are significantly different from the requirements of the empirical method.

⁶⁵¹ See *supra* note 632.

The theoretical and empirical methods will be applied to the provisions in the *GATT 1994*, *SCM Agreement* and *AoA* in the next section to determine whether or not there is conflict among these three Agreements.

III.3 The Application of the Theoretical and the Empirical Methods to Identify Whether There Is Conflict among the *AoA*, *SCM Agreement* and *GATT 1994*

Now, we turn to the main questions in this study, presented in the introduction, about the limits to the challengeability of agricultural subsidies upon the expiry of the Peace Clause. Whether there is a conflict between the regulation of each type of agricultural subsidy (green, non-green and export) will be looked at. If there is none, the limits to the challengeability of agricultural subsidies upon the expiry of Peace Clause will be delineated according to the cumulative application of the *AoA*, *SCM Agreement* and *GATT 1994*.⁶⁵²

III.3.1 The Application of the Theoretical Method to Green Box Measures

The theoretical method's first threshold for a conflict to exist requires that the agreements or the provisions that regulate green box measures a) concern the same parties, b) have the same substantive subject matter and c) have mutually exclusive obligations.⁶⁵³ Unless all three of these conditions are met, there is no conflict.

The agreements that regulate green box subsidies cover the same parties, because the *GATT 1994*, the *AoA* and the *SCM Agreement* are different agreements but part of the same

⁶⁵² For didactic purposes, the use of the theoretical and practical methods for green, non-green and export subsidies will take into account all *AoA* substantive provisions, *SCM Agreement* Part II and III and *GATT* Art. XVI, which are the main provisions for the challengeability of agricultural subsidies.

⁶⁵³ *Indonesia – Autos supra* note 234 at 14.28.

treaty⁶⁵⁴ which was the result of the Uruguay Round. Therefore, they had the same signatories. However, the three agreements do not have the same subject matter and do not require mutual exclusivity. For this reason, the first condition is not fulfilled, which means that there is no conflict among the treaties and the provisions that regulate green box subsidies. Consequently, they can be cumulatively applied.

Regarding the second condition, even though the three Agreements are interrelated, their subject matter is not the same. The *GATT 1994* has a vast magnitude of rules that range from establishing general principles of international trade to defining schedules of concessions. The *AoA* institutes quantitative commitments to regulate the level of support given to agricultural products, and the *SCM Agreement* qualitatively defines situations where subsidizing is authorized or prohibited. Each provision of these Agreements reflects the idiosyncratic nature of the agreement it belongs to.

It could be said that, because these Agreements are interrelated, they have certain areas of common regulation, but that does not mean that they have a mutually exclusive obligation to regulate a subject. In *Indonesia – Autos*, a mutually exclusive obligation meant a conflict when two or more norms contained obligations that could not be complied with simultaneously. *AoA* Annex II defines green box subsidies as support measures exempt from the reduction commitments that have to have no or minimal trade-distorting effects. There is no provision for the challengeability of this type of subsidy in the *AoA*. The *SCM Agreement* defines subsidies in general and determines which subsidies are actionable and prohibited and does not specifically refer to green box measures. Therefore, in terms of green non-distortive measures, there is no mutual obligation to, because each one has a different set of rules. One of the quantitative obligations established in the *AoA* is that of complying with the reduction commitments, whereas

⁶⁵⁴ See footnote 641.

the *SCM Agreement* requires qualitative actions from its signatories to perform an action or to prohibit conduct, such as subsidizing contingent upon export performance.

Owing to the fact that divergence of obligations is not enough to characterize a conflict, the second threshold is also related to the mutual obligation requirement that establishes that one treaty or provision must not hinder compliance with another at the same time. Therefore, there is a conflict when two or more treaties, or provisions, contain obligations that cannot be complied with simultaneously.

The regulation of green box subsidies in the *AoA*, *SCM Agreement* and *GATT 1994* can be complied with at the same time because, while *AoA* Annex 2 defines green box subsidies, the *SCM Agreement* sets legal limits for subsidization. These Agreements are interrelated not only because they are parts of the same treaty but also because there are cross-references in their texts; however, this does not mean that they cannot be complied with at the same time. It makes the challengeability of green box subsidies that cause adverse effects possible. Article XVI of the *GATT 1994*, which regulates subsidies, has more general and less stringent limitations for subsidization than the *SCM Agreement*. Therefore, the three Agreements can be simultaneously applied. Compliance with the provisions of one of the Agreements does not hinder the application of the other agreements. On the contrary, they are complementary.

The third threshold established by the Appellate Body report in *Guatemala – Cement I*⁶⁵⁵ was that, if two agreements or provisions can be complementary to each other, the more specific prevails only if there is an inconsistency in the more generic one. In regards to the regulation of agricultural subsidies, the *AoA* is a more specific agreement than the *SCM Agreement*, which, in turn, is more specific than the *GATT 1994*. There is no inconsistency in either the *GATT 1994* or the *SCM Agreement* that could justify the sole regulation of agricultural subsidies by the *AoA*.

⁶⁵⁵ *Guatemala – Cement I* *supra* note 649 at para. 65.

It could be said that the rationale of the *AoA* is that a subsidy satisfying all the requirements of Annex 2 could be used without limitation. Furthermore, following the same rationale, imposing extra constraints (such as the provisions of the *SCM Agreement* or Article XVI of *GATT 1994*) on *AoA* green box subsidies could excessively limit the right of a member to grant green box agricultural subsidies. By way of this reasoning, some argue that the *SCM Agreement* and Article XVI of *GATT 1994* should not apply to green box agricultural subsidies.

However, as discussed above, there is no conflict between the *AoA* and the *SCM Agreement* and, for this reason, they have to be applied together. As such, if green box subsidies were meant to be used without limits upon expiry of the Peace Clause, the *SCM Agreement* provisions would be violated, because they clearly define the limits to subsidization for all prohibited and actionable subsidies.

Another argument against the simultaneous use of the three Agreements is that the criteria set forth in Annex 2 to the *AoA* do not lead to a violation of Part III of the *SCM Agreement*. If the green box measure does not cause adverse effect to any other Member, it does not lead to a violation. However, if it harms another member, there is a violation, and then, the *SCM Agreement* applies.

AoA Art. 6 states that green box measures are not subject to reduction commitments, and Annex 2 defines green box measures. Part III of the *SCM Agreement* establishes limits for the actionability of any domestic support measures that cause adverse effects. If the green support measures harm, nullify or impair the interest of any other Member, they have to be challenged. Moreover, because green box subsidies do not have to comply with the reduction schedules, if they cause an adverse effect, they are not limited under the *AoA*; therefore, the application of the limits provided for by the *SCM Agreement* are necessary. The limit for the actionability of green

box subsidies, in this case, are set out in *SCM Agreement* Article 5, which establishes that no Member should cause adverse effects to the other through the use of the subsidies defined in *SCM Agreement* Arts. 1 and 2.

These Articles define subsidies as a financial contribution that has to be specific. Therefore, if a green box subsidy is a specific financial contribution that is causing an adverse effect to a WTO Member according to the concept of subsidy and specificity already analyzed in Part II of this study, it can be challengeable under the *SCM Agreement*. Otherwise, the agreements would not be complementary and would not be a single undertaking, *AoA* Article 21.1 would be violated and there would not be an inseparable and coherent package of treaties.

It can also appear, after a shallow legal analysis, that the requirement present in Annex 2 to minimize trade-distorting effects is not compatible with the *SCM Agreement*'s obligation to not cause adverse effects. The rules agreed upon in pursuit of the same aim, as previously stated, differ considerably from one to the other. Part III of the *SCM Agreement* contains detailed limits on agriculture subsidization that restrains their use through the use of the concepts of injury and serious prejudice. Annex 2 defines green box subsidies. For this reason, even though Annex 2 establishes that a domestic support measure shall "have no or at most minimal, trade-distorting effects, or effects on production," it does not mean that Part III of the *SCM Agreement* cannot be applied if there are trade-distorting effects.

Besides, as seen, some distortive measures were improperly placed under the green "cloth" through the process called "box shifting." The reality is that, just because a subsidy is classified as a green box measure, it does not necessarily mean that it does not distort trade. If it does not, it cannot be challenged under the *SCM Agreement*, because an adverse effect is a

requirement for actionability. If it does distort, the green box measure can be legally challenged under the provisions of the *SCM Agreement*.

Another argument against the application of the cumulative interpretation of the agreements would be that the *AoA* implicitly makes green box subsidies non-actionable, because they do not distort trade. Besides, a green box subsidy would never meet the standards of the concept of “serious prejudice,” and if green box subsidies could be actionable, *AoA* Annex 2 would be useless or meaningless.

Despite all the legal reasoning already presented, the conclusion above fails to distinguish between legality and challengeability. As was previously mentioned,⁶⁵⁶ challengeability means any challenge under the WTO system. If a subsidy is a challengeable, it does not mean that it is illegal. “The Peace Clause used to constrain challengeability, but did not regulate legality.”⁶⁵⁷ Green box subsidies are legal, but this does not mean that they cannot be challenged if they cause any sort of adverse effect.⁶⁵⁸ Serious prejudice is only one of the three possible adverse effects already mentioned in this study.

It also could be said that the *AoA* preamble clearly states that one of its goals is “to provide for substantial progressive reductions in agricultural support and protection sustained over an agreed period of time.”⁶⁵⁹ For this reason, applying the *SCM Agreement* to the *AoA* could undermine this purpose, because in this case, the *SCM Agreement*, whose goal is to eliminate

⁶⁵⁶ See n. 6.

⁶⁵⁷ *Ibid.*

⁶⁵⁸ Several authors agreed with this difference between challengeability and legality. See Steinberg, “Peace Clause” *supra* note 7 and Siuves, H.N. “The expiry of the peace clause on agricultural export subsidies – the outlook post-Cancun” (2004) 31 *Legal Issues of Economic Integration* 25, at 32–34 in Wouters, Jan & Coppens, Dominic. “An Overview of the *Agreement on Subsidies and Countervailing Measures* – Including a Discussion of the *Agreement on Agriculture*” *Working Paper No 104 from the Institute for International Law* (Leuven: Institute for International Law K.U. Leuven, 2007) at n. 484.

⁶⁵⁹ *AoA* Preamble at para. 3.

distortive subsidies, would pre-empt the *AoA*'s purpose of merely reducing agricultural subsidies.

One of the main goals of the *SCM Agreement* is not to eliminate subsidies, but to make the distortive ones challengeable. Therefore, in this sense, the *SCM Agreement* and the *AoA* have the same goals—to diminish trade restrictions. Besides, the fact that one of the goals of the *AoA* is to reduce agricultural subsidies does not mean that they cannot be challenged. In this manner, challengeability under the *SCM Agreement* helps to reach the *AoA*'s goal to reduce subsidies, because challengeability is one possible way to limit distortive agricultural subsidization.

The conclusion is that an analysis by the empirical method shows that there is no conflict among the agreements that regulate green-box subsidies.

III.3.2 The Theoretical Method Applied to Green Box Measures

According to the theoretical method applied by this study, there are four types of international norms that can bring about a situation of conflict: command, prohibition, permission and exemption. The situations of conflict normally occur between a) two norms of command, b) one norm of command and another of prohibition, c) one norm of command and another of exemption and d) one norm of prohibition and another of permission.⁶⁶⁰

SCM Agreement Part II prohibits export subsidies, and Part III states that subsidies “should not cause ... adverse effects to the interests of other Members”; otherwise, they are actionable. Part III is of more relevance for green box measures, because Part II regulates exports and subsidies contingent upon the use of domestic over imported goods. Because Art. 5 in Part III uses the phrase “no Member should cause,” this provision is prohibiting WTO

⁶⁶⁰ See p. 245- 246.

Members from providing subsidies that distort trade and cause adverse effects, which means that this is a prohibition provision according to the theoretical method. Art. 5 has a paragraph stating that it does not apply to agricultural subsidies because of the shield of the Peace Clause. Because of the expiration of *AoA* Art. 13, this paragraph no longer is applied and, consequently, does not change the prohibitive nature of the provision.

AoA Part IV Art. 6 establishes that Annex 2 defines green box subsidies. Art. 6 establishes that domestic reduction commitments shall apply to all domestic agriculture, with three exceptions: some measures for developing countries to encourage diversification from growing illicit narcotic crops, support under *de minimis* levels and green box measures defined in Annex 2. In turn, Annex 2 includes a specific list of green box subsidies that have minimal or non-distortive effects and that should be exempt from reduction commitments. The title of *AoA* Annex 2 is “Domestic Support: The Basis for Exemption from the Reduction Commitments.” Therefore, it is clear, with the theoretical method, that *AoA* Annex II is an exemption norm. Its purpose is to exempt green box measures from reduction commitments established in Part IV of Members’ schedules.

The conclusion with the theoretical method is that a norm of prohibition does not conflict with a norm of exemption; therefore, there is no conflict between the *AoA* and the *SCM Agreement* regarding regulation of green box subsidies. Regarding *GATT 1994* Art. XIV, it is important to observe that the General Interpretative Note to Annex 1A states that a provision in any Annex 1A agreement prevails over any *GATT 1994* provision in the case of a conflict.⁶⁶¹

⁶⁶¹ It is relevant to note that the *AoA*, *SCM Agreement* and *GATT 1994* are three different Agreements from the same treaty. The concept of conflict in this research applies to different “norms” that comprise different treaties, Agreements or different provisions of the same treaty. This is the same concept applied by the WTO cases when they analyze conflict among different Agreements or different provisions of different Agreements. It is not included in the concept of “norm” pre-normative rules (drafts, *travaux préparatoires*, written intentions).

Therefore, it is clear that the provisions of the *AoA* or *SCM Agreement* prevail over *GATT 1994* provisions in the case of a conflict, but in this case, there is no conflict.

GATT 1994 Art. XVI only mentions that, if a subsidy caused serious prejudice, Members could discuss the possibility of limiting such subsidy. It did not establish a system to regulate or limit domestic subsidization and, consequently, did not prohibit such subsidies. Therefore it could be said that the *GATT 1994* was a permission norm regarding green box subsidies, which purportedly do not distort trade. In the theoretical method, a permission norm is consistent with an exemption norm; consequently, the application of this method shows that there is no conflict between *AoA* regulations for green box subsidies and the *GATT 1994*.

It could be said that the permission provision of *GATT 1994* Art. XVI could conflict with the prohibition provision of Part III of the *SCM Agreement*; however, they do not conflict. First, neither Art. XVI nor the *SCM Agreement* directly regulates green box measures; therefore, the subjects of regulation are different. *GATT 1994* does not specifically authorize green box subsidization, because there is no specific reference in the Agreement to this type of subsidy and because the *GATT 1994* tended to limit subsidies that might cause serious prejudice. On the other hand, the *SCM Agreement* sets out the limits for the actionability of subsidies that distort trade. A conflict would occur if the *GATT 1994* specifically authorized domestic subsidies that could be classified as green box measures and if the *GATT 1994* had not established any form of consultations to try to limit subsidization that can cause serious prejudice.

III.3.3 The Empirical Method Applied to Non-green Box Measures

As for green box subsidies, the legal boundaries of challengeability after the expiry of the Peace Clause must also be redefined for non-green box subsidies. For this purpose, it must be determined whether conflict can be found among the agreements that regulate non-green box subsidies. The first threshold of the empirical method requires the conditions that the agreements that regulate non-green subsidies have a) the same parties, b) the same subject matter and c) a mutually exclusive obligation. Since the agreements that regulate green and non-green box measures are the same (*AoA*, *SCM Agreement* and *GATT 1994*), one can conclude that the agreements regulating non-green box subsidies also do not conflict and can be applied in accordance with the cumulative principle.

The second threshold (the subject matter of the three Agreements must be different to not characterize a conflict) of the empirical method is also reached. The *AoA*, *SCM Agreement* and *GATT 1994* can be simultaneously applied to regulate non-green box subsidies according for the same reasons as those in the test for green box measures. The *GATT 1994* is a general agreement whose subject of regulation is vast and ample and ranges from establishing general principles of international trade to defining schedules of concessions. *AoA* Article 6 defines amber box subsidies as support measures submitted to reduction commitments contained in Part IV of Members' Schedules and blue box subsidies as direct payments under production-limiting programs that are not subject to reduction commitments if they are based on a fixed area or are made on 85% or less of the base level of production. *SCM Agreement* Part III presents legal limits for the subsidization of non-green subsidies that cause adverse effects, which makes the

actionability of non-green box subsidies possible, even under the limits based on what was decided during the 1992 marketing year.

The third threshold (whether the agreements or provisions can be complementary to each other with the more specific prevailing only if there is an inconsistency in the more generic one) is also reached, since the agreements that regulate green box subsidies are the same for non-green subsidies. For non-green box subsidies, there is neither an inconsistency in the *GATT 1994* nor in the *SCM Agreement* that could justify the sole regulation of these measures by the AoA. This means that there is no conflict among these Agreements regarding the regulation of non-green subsidies.

III.3.4 The Theoretical Method Applied to Non-green Box Measures

The same test that was applied for green box subsidies will be applied here to identify the nature of the agreements that regulate non-green subsidies to verify whether there is a conflict among them.

SCM Agreement Part III Art. 5 can be used to challenge non-green subsidies that cause adverse effects, and it has already been determined in this study that it is a prohibition provision according to the theoretical method.

AoA Part IV, Art. 6, establishes that reduction commitments shall apply to all amber box subsidies that are support measures contained in Part IV of Members' schedules. It is a command provision regarding the application of reduction commitments for all amber box subsidies. The command is that all amber box measures that are considered trade distortive have to be submitted to reduction commitments. A shallow analysis would show that this command provision of *AoA*

Art. 6.1 conflicts with the *SCM Agreement* prohibition provision that also regulates amber box subsidies. However, this conclusion does not survive a deeper analysis.

The conflict between a command and a prohibition provision in the theoretical method occurs when the command states that a Member shall do "X," and the prohibition provision states that a member shall not do "X." This means that a conflict will only occur if command and prohibition provisions regulate the same subject. In the present case, the command provision of the *AoA* does not regulate the same subject as the prohibition provision of the *SCM Agreement*. A conflict would occur only if, for example, the *SCM Agreement* determined that reductions commitments should not apply to amber box measures or if the *AoA* stated that amber box measures that caused an adverse effect were not actionable.

AoA Art. 6.1 materially regulates amber box subsidies through a command provision, and *SCM Agreement* Art. 5 states that all subsidies, not only amber box measures, are actionable through a prohibition provision. Both provisions are not regulating the same subject. While *AoA* states that Members shall do "X," the *SCM Agreement* establishes that Members shall not do "Y"; therefore, there is no conflict between the *AoA* and the *SCM Agreement* regarding the regulation of non-green box measures.

Regarding the *GATT 1994*, even though Art. XIV had a mention that, if a subsidy caused serious prejudice, Members could discuss the possibility of limiting such subsidy, this cannot be considered as a prohibition provision. According to the theoretical method, a prohibition provision is a "shall not do" provision. The *GATT 1994* did not establish that domestic support that causes adverse effects should not be given. It stated that Members should discuss the possibility of limiting subsidization, which is not a prohibition. It is still a permission provision under specific circumstances; therefore, according to the theoretical method, the *GATT 1994*'s

regulation of amber box is *included* in and does not conflict with the *AoA* command provision that regulates amber box measures. The *GATT 1994* and the *SCM Agreement* provisions regarding regulation of non-green box measures do not conflict for the same reason that they do not conflict in regulating green box measures. The subjects of regulation are not the same and, even though *GATT 1994* Art. XVI cannot be considered as a prohibition provision, it calls for consultations with the possibility of limiting the subsidization that caused the serious prejudice.

III.3.5 The Empirical Method Applied to Export Measures

The agreements that regulate export subsidies involve the same parties, because, as was seen, they are parts of the same treaty. They do not have the same subject matter and do not have an obligation for mutual exclusivity. For this reason, there is no conflict among the provisions that regulate export subsidies . Therefore, they can be cumulatively applied.

The second threshold for a conflict to exist is also not reached, because the *AoA*, *SCM Agreement* and *GATT 1994* can be simultaneously applied to regulate export subsidies. This is corroborated by the cross-references between *SCM Agreement* Art. 3.1 (a) and (b), which prohibits export subsidies, and *AoA* Arts. 8 and 9, which regulates them, as it is going to be seen in the analysis of the theoretical method.

The third threshold for a conflict is also not reached, since the agreements that regulate green and non-green subsidies are the same as those regulating exports. Regarding export subsidies, there is neither inconsistency in the *GATT 1994* nor in the *SCM Agreement* that would hinder the application of the *AoA* to agricultural export subsidies; therefore, there is no conflict among the Agreements regarding the regulation of export subsidies.

III.3.6 The Theoretical Method Applied to Export Measures

SCM Agreement Part III, Art. 3.1, clearly states that subsidies contingent upon export performance or upon the use of domestic over imported goods “shall be prohibited.” Therefore, it is a prohibition provision according to the theoretical method. *AoA* Part V regulates export commitments. Art. 8 states that Members “shall not” provide export subsidies otherwise than in conformity with the commitments specified in Members’ schedules and in the *AoA*. Art. 9 provides a *numerus clausus* list of export subsidies that can be given, subject to *AoA* reduction commitments. Art. 10 states that export subsidies not listed in Art. 9 “shall not” be applied in a manner that leads to the circumvention of export subsidy commitments.

AoA Arts. 8 and 10 prohibit export subsidies that are not applied under the limits or that circumvent the commitments established in the Agreement. Art. 9 determines a list of export subsidies subject to reductions commitments, which means it exempts some export subsidies that can be given if they are under the Schedule’s limits. Therefore, Arts. 8 and 10 are prohibition provisions, and Art. 9 is an exemption provision. Neither of them conflict with the prohibition provision of *SCM Agreement* 3.1. According to the theoretical method, the two prohibitions do not conflict, and the exemption of *AoA* Art. 9 is *included* in the prohibitions of *AoA* Arts. 8 and 10 and *SCM Agreement* Art. 3.1. As a result, the *SCM Agreement* and *AoA* can be cumulatively applied to regulate export subsidies.

Art. 3.1 could also be considered as an exemption norm in comparison to the *AoA*, because it also states that “[e]xcept as provided in the *Agreement on Agriculture*.” Even in this case, *SCM Agreement* Art. 3.1 would conflict neither with *AoA* Arts. 8 and 10 nor with Art. 9.

The reason is that, according to the theoretical method, a prohibition provision *includes* an exemption provision, and two prohibition provisions do not conflict.

Moreover, *SCM Agreement* Art. 3.1's exception regarding the *AoA* does not change the prohibition nature of this article. Because the *AoA* also prohibits export subsidies under Arts. 8 and 10, the *SCM Agreement* and *AoA* not only do not conflict but also complement each other, even though *AoA* Art. 9 exempts some export subsidies within certain limits.

Regarding the *GATT 1994*, Art. XVI states that subsidies "shall not" be given in a manner that results in a contracting party's having more than an equitable share of the world export trade in that product. It is a prohibition provision and, for this reason, does not conflict with the prohibition of *SCM Agreement* Art. 3. It could be said that the flat and absolute prohibition of *SCM Agreement* Art. 3.1 for export subsidization conflicts with *GATT 1994* Art. XVI, because this provision only limited export subsidies that gave to the subsidizing Member "more than an equitable share of the world export trade" in the subsidized product, which is not a flat prohibition.

The fact that *SCM Agreement* Art. 3.1 is a flat prohibition for export subsidies and *GATT 1994* Art. XVI is not does not change the prohibition nature of both provisions. The conflict would exist if one of the provisions specifically authorized export subsidization, which did not occur. Export subsidies not prohibited under *GATT 1994* Art. XVI are those that do not give a more than an equitable share of the world trade market of the subsidized product to the subsidizing Member. If an export subsidy does not change the share of the world trade market of the subsidized product, most likely it will not cause an adverse effect to other Members. In this case, there would be no interest in the challengeability of this export subsidy, neither under *GATT 1994* Art. XVI nor under *SCM Agreement* Art. 3.1.

The fact that the *SCM Agreement* has more stringent provisions that might include export subsidies that were not included in the prohibition of the *GATT 1994* does not mean that both provisions conflict with each other, but it is an indication that *SCM Agreement* Art. 3.1 *includes* the prohibition of subsidies included in *GATT 1994* Art. XVI plus other types of export subsidization not included in this provision. Because both provisions prohibit export subsidies, *GATT 1994* Art. XVI does not conflict with *AoA* Art. 8 and 10 prohibition provisions, either, and *includes* the exemption provision of *AoA* Art. 9.

It has been seen, by applying the empirical and theoretical methods, that there is no conflict among the *GATT 1994*, *SCM Agreement* and *AoA* regarding the regulation of agricultural subsidies. The conclusion is that they have to be cumulatively applied to determine the limits of the challengeability for agricultural subsidies after the Peace Clause. Now that these limits have been determined, the next section defines the current regime for the challengeability of agricultural subsidies.

III.4 The Cumulative Application of the *AoA*, *SCM Agreement* and *GATT 1994* to Define the “New” Limits of Challengeability for Agricultural Subsidies upon the Expiry of the Peace Clause

It has been determined there is no conflict among the WTO agreements that discipline agricultural subsidies, and this fact has indicated which approach to use to interpret the relationships between the *AoA*, *SCM Agreement* and *GATT 1994*. As a result, how each one of these Agreements relates to the other to shape the new boundaries for the challengeability of agricultural subsidies after the expiry of the Peace Clause should be analyzed.

This expiry changed the limits on the challengeability of all agricultural subsidies, because the *SCM Agreement* and the *GATT 1994* are currently applicable to all agricultural

subsidies. The subsidies are challengeable under *SCM Agreement* Part II, III and V and *GATT 1994* Arts. XVI and XXIII 1(b). Currently, agricultural subsidies can also be countervailed and submitted to non-violation claims.⁶⁶² The limits to the challengeability of each WTO agreement that regulates agricultural subsidies were evaluated in Part II of this study, but the confluent zone of regulations for the challengeability of agricultural subsidies will be analyzed in this section.

III.4.1 The Challengeability of Agricultural Subsidies under the *SCM Agreement*

There is no explicit rule that determines how agricultural subsidies will be challengeable under the *SCM Agreement*. Marc Benitah calls this absence “the ambiguous silence as to the link between two texts.” According to him, this silence could be a technique that could be used to the advantage of the subsidizing or the affected country and is normally perceived as leaning towards the attenuation of entitlements granted to the affected country.⁶⁶³

He gives some examples of what would be considered as “ambiguous silence,” one being the “double price level” criterion of the *GATT 1994*. *GATT 1947* Art. XVI:4 prohibited non-agricultural export subsidies and added, according to Benitah, an attenuation: “which subsidy results in the sale of such product for export at price lower than the comparable price charged for the like product to buyers in the domestic market.”⁶⁶⁴ According to the author, the double price level was difficult to apply and thus resulted in the provision’s not being included in the TRSC. This, said the author, characterizes an ambiguous silence.

⁶⁶² It should be noted that non-violation claims are obsolete, because the configuration of a non-violation claim was designed to protect the schedules of concessions given in the past. Currently, any challenge that is not supported by an allegation of violation of specific provisions of the WTO Agreements most likely will not succeed.

⁶⁶³ Benitah, *Law of Subsidies supra* note 87 at 62.

⁶⁶⁴ *GATT* Art. XVI:4.

In his work, Marc Benitah describes what he calls “techniques of attenuation,” which are ways to attenuate entitlements granted to the party seeking to defend itself against the “adverse effects” of pollution in domestic law or of subsidies in international economic law.”⁶⁶⁵ In this context, ambiguous silence is one of the techniques of attenuation that the author points to, because it can be used to defend the subsidizing Member against possible allegations of violation by affected Members.

The purported “silence” between the *SCM Agreement* and the *AoA* cannot be considered a pre-conceived technique because it goes against the negotiating history of the agreements. Section III.2.1 studied the background of the Peace Clause and noted that it was used as a lever for the EC to accept the *AoA* provisions to reduce agricultural subsidies. Therefore, the Peace Clause is evidence that negotiators knew that agricultural subsidies could be challenged under the *SCM Agreement* and, as a result, there was no “intentional silence” about the relationship between these two Agreements.

Besides, *AoA* Art. 21.1 states “The provisions of *GATT 1994* and of other Multilateral Trade Agreements in Annex 1A to the WTO Agreement shall apply subject to the provisions of this Agreement.” There is a clear manifestation in the *AoA* that this Agreement can be concomitantly applied with the *GATT 1994* and other WTO agreements, therefore the *AoA* is not so “silent” about its interpretation and application concerning other WTO agreements.

Actually, the WTO is not silent at all about the correlation among its agreements, because the General Interpretative Note to Annex 1A foresees a possible situation of conflict between the *GATT 1994* and other WTO Annex 1A agreements and clearly states that the provisions of the other WTO Annex 1A agreements prevail over *GATT 1994* provisions in the event of a conflict. The example given by Benitah regarding the *GATT 1947* provision of a “double price level” was

⁶⁶⁵ Benitah, *Law of Subsidies supra* note 87 at 1.

already examined in Part I, chapter I.2, of this study, and the conclusion was that *GATT 1947* Art. XVI:4 was a difficult provision to be applied. Its market-effect component made challengeability difficult during the *GATT 1947* years.

There was no record of a *GATT 1947* case challenging this provision; as a result, it was predictable that it would not be repeated in the TRSC. Besides, the *SCM Agreement* consolidated the tendency established by the TRSC to place market-effect provisions in countervailing duties' regulation and non-market-effect provisions in subsidies regulation. Finally, there is no "ambiguous silence" about the *AoA* and *SCM Agreement* regulation. As it is confirmed by *AoA* Art. 21.1. these Agreements are part of a complete, indivisible and intricate system.

Furthermore, the several references to the Peace Clause in the *SCM Agreement* prove that not only was there no silence about the relationship between the *SCM Agreement* and the *AoA*, but also that the limits to challengeability were also determined by these references. *SCM Agreement* Art. 5, which indicates how to challenge actionable subsidies, and Art. 7, which provides remedies for them, specifically mention that the provisions did not apply to agricultural subsidies because of the Peace Clause.⁶⁶⁶ This means that, after the Peace Clause expired, *SCM Agreement* Art. 5 and 7 applied to agricultural subsidies. It does not mean that the *SCM Agreement* can adjudicate every *AoA* substantive provision. However, after the expiry of the Peace Clause agricultural subsidies that are prohibited or actionable under *SCM Agreement* Arts. 3 and 5 can be challenged under the *SCM Agreement* *SCM Agreement* Arts. 4 and 7. As mentioned before, in *US – Subsidies on Upland Cotton* the panel found that the US had failed to

⁶⁶⁶ *SCM Agreement* Art. 5 states "[t]his article does not apply to subsidies maintained on agricultural products as provided in Article 13 of the *Agreement on Agriculture*" and *SC* Art. 7 states [e]xcept as provided in Article 13 of the *Agreement on Agriculture*, whenever a Member has reason to believe that any subsidy referred to in Article 1 ... results in injury ... such Member may request consultations with such other Member.

comply with its obligation under *SCM Agreement* Art. 7.8 to take appropriate steps to remove cotton subsidies.

Besides, several references in the *SCM Agreement* to the *AoA* are also evidence that there was no intentional silence in the WTO agreements. *SCM Agreement* Art. 3 states that “[e]xcept as provided in the *Agreement on Agriculture*,” export subsidies should be prohibited, and Art. 5 specifically declares that “[t]his article does not apply to subsidies maintained on agricultural products as provided in Article 13 of the *Agreement on Agriculture*.” There are also several mentions in the *SCM Agreement* of concepts such as subsidy⁶⁶⁷, nullification or impairment⁶⁶⁸ and serious prejudice⁶⁶⁹ and a statement to the effect that these terms are used in the same sense as they are in the *GATT 1994*, in a clear reference that relates to the Agreements.

Other evidence that the *SCM Agreement* and *AoA* were intentionally negotiated to operate together regarding the challengeability of agricultural subsidies is the requirement to create special dispute settlement mechanisms for prohibited and actionable subsidies, defined in *SCM Agreement* Arts. 4 and 7—examined in chapter II.5 of this study. As has already been observed, Art. 7 has a specific mention that the Peace Clause excluded agricultural subsidies from this special mechanism for settling actionable subsidy disputes. The same conclusion as above applies here: *SCM Agreement* Art. 7 was meant to apply to agriculture after the expiry of the Peace Clause.

It is interesting to note, however, that *SCM Agreement* Art. 4 has no mention of the Peace Clause. *AoA* Art. 13 restrained the challengeability of *SCM Agreement* Art. 3, 5 and 6, but did not restrain it under Art. 4. The conclusion is that export subsidies were possibly vulnerable to the special procedures provided for in *SCM Agreement* Art. 4, even during the period of the

⁶⁶⁷ See *SCM Agreement* Art. 1.1(a)(2).

⁶⁶⁸ See *SCM Agreement* Art. 5(b).

⁶⁶⁹ See *SCM Agreement* Art. 5(c).

Peace Clause. The fact that Art. 7 mentions exceptions for agricultural subsidies, and Art. 4 does not, means that the *SCM Agreement* intentionally opened a small window for the challengeability of export agricultural subsidies during the peace period.

However, this possible remedy was never applied when the shield of the Peace Clause existed. First, it would be difficult to challenge export agricultural subsidies under *SCM Agreement* Art. 4, which provided a remedy for prohibited subsidies because the Art. 3 chapeau stated that “[e]xcept as provided in the *Agreement on Agriculture*, the following subsidies within the meaning of Article 1, shall be prohibited.” Second, during the years when challengeability was protected by the shield of the Peace Clause, it was clear there were two different regimes for the challengeability of subsidies: one for non-agricultural goods and one for agricultural products whose challengeability was significantly restrained by the Peace Clause, especially for green box subsidies.

Even though it is clear that negotiators intended *SCM Agreement* Parts II, III and V to apply to agricultural subsidies after the expiry of the Peace Clause, in order to be challengeable under these provisions, agricultural subsidies have to fulfil all the *SCM Agreement* general requirements for challengeability. In this section, it will be seen whether agricultural subsidies fit under the *SCM Agreement* definition of subsidies and whether they can be considered specific according the criteria set forth in *SCM Agreement* Part II, III and V.

III.4.1.1 Agricultural Subsidies and the *SCM Agreement*'s Definition of Subsidy

Agricultural subsidies can be challenged under the *SCM Agreement* if Art. 1.1, which contains a definition of a subsidy, can be applied to subsidies on agricultural products. The *SCM*

Agreement states that a subsidy “shall be deemed to exist if there is a financial contribution by a government or any public body within the territory of a Member,” where:

- (i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity injection), potential direct transfers of funds or liabilities (e.g. loan guarantees);
- (ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits);
- (iii) a government provides goods or services other than general infrastructure, or purchases goods;
- (iv) a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions illustrated in (i) to (v) above which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments;”⁶⁷⁰

Agricultural support measures constitute financial contribution pursuant to Article 1.1(a)(1) of the *SCM Agreement* because they include “governmental contribution within the territory of one Member.” *AoA* Art. 1 brings a definition list of the terms used in the agreement. Letter (a) defines “Aggregated Measurement of Support” [AMS] as the annual level of support expressed in monetary terms. Letter (d) defines “Equivalent Measurement of Support” as a type of annual level of support expressed in monetary terms. Therefore, the definitions provided by the *AoA* prove agricultural subsidies can involve a direct or indirect financial contribution.

In “*Korea – Various Measures on Beef*” the complainants argued that Korea’s current total AMS provided in the notifications were calculated improperly, and; therefore, the methods of calculation of the AMS levels of support were discussed. The panel decided that Korea’s current total AMS had exceeded its commitments levels and violated *AoA* Art. 3.2.⁶⁷¹ The discussion was about whether AMS levels calculated according to *AoA* Annex 3 had precedence

⁶⁷⁰ *SCM Agreement* Art. 1.1 (a)(1)(i), (ii), (iii) and (iv).

⁶⁷¹ Panel Report, *Korea – Measures Affecting Imports of Fresh, Chilled and Frozen Beef*, (2001) WT/DS161/R, WT/DS169/R, at para. 843 adopted 10 January 2001, as modified by Appellate Body Report WT/DS161/AB/R, WT/DS169/AB/R, DSR 2001:I, 59 [*Korea – Various Measures on Beef*].

over the methods calculated according to the part IV of Member's schedules. The panel decided that the AMS annual levels should be calculated according to Annex 3 alone.⁶⁷²

The discussion, however, was about the methodology to calculate the AMS total levels and not about whether the support calculated in terms of AMS could be considered a "financial contribution." Therefore, it is clear that agricultural subsidies can be considered a "financial contribution" that is calculated in terms of AMS. The proof is that the agricultural subsidies can be not only direct financial support but also other forms of subsidies as well, such as revenues foregone as the *US – FSC* case demonstrated.⁶⁷³

It is worth recalling that the quantification of market price support, in AMS terms, is not simply based on budgetary outlays. Market price support as defined in *AoA* Annex 3 can exist even where there is no financial contribution by a government or public body. As well, *SCM Agreement* Art. 1 establishes forms of subsidies other than financial contributions, such as forgone revenue, provision of goods or services other than infrastructure, the purchase of goods and payments to funding mechanisms. This means that indirect financial contributions to agriculture can also be considered as a form of subsidy by the *SCM Agreement*.

In *US – FSC*, the AB noted that the *AoA* "does not contain a definition of the terms 'subsidy' or 'subsidies.'" According to the AB, quoting a decision in *Canada – Dairy*, a case is related to subsidies when it "involves a transfer of economic resources from the grantor to the recipient for less than full consideration."⁶⁷⁴ In order to reach this definition, the AB used the

⁶⁷² *Ibid.* at para. 114

⁶⁷³ *AoA* Art. 1(c) states that budgetary outlays include revenue foregone that is one of the forms of subsidy expressly mentioned in the *SCM Agreement*.

⁶⁷⁴ Appellate Body Report, *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products*, WT/DS103/AB/R, WT/DS113/AB/R and Corr.1, para. 87 adopted 27 October 1999, DSR 1999:V, 2057 [*Canada – Dairy*] cited in *US – FSC* *supra* note 405

concept of subsidy of *SCM Agreement* Art. 1.1, which states that a “subsidy” exists where the grantor makes a “financial contribution” that gives a “benefit” to the recipient.⁶⁷⁵

The AB upheld the panel’s decision that the “alleged subsidies ... involve[d] a transfer of resources through the foregoing of revenue.” It stated that agricultural subsidies, just as defined in *SCM Agreement* Art. 1.1(a)(1)(ii), could also constitute government revenue that is forgone or not collected. The AB stated that the “fiscal treatment of agricultural product is not materially different, from the present purposes, from the fiscal treatment of products falling within the scope of application of the *SCM Agreement*.”⁶⁷⁶

Regarding the part of the subsidies’ definition that states that subsidies are given by “a government or a public body that acts in the name of the government,” the *AoA* regulates several types of subsidies and refers to Members as active agents of subsidization. The term “Members” in this case can be replaced by governments or public bodies controlled by the government. There is a presumption that most subsidies (agricultural or not) are given by governments or a public body. There are WTO disputes discussing the limits of the concept “public body” previously analyzed in this study. In *Korea – Vessels* it was determined a “public body” is an entity controlled by the government.⁶⁷⁷ A concession of a benefit can be presumed from an agricultural subsidy as well as from a non-agricultural subsidy.

Regarding the concept of a “benefit that is conferred” the AB upheld the panel’s decision in *US – FSC* that the term “‘benefit’” under Article 1.1(b) of the *SCM Agreement* also involved a ‘benefit’ under Article 1.1(b) of that Agreement [the *AoA*].”⁶⁷⁸ The AB considered that the exemptions provided by the FSC measures that constituted subsidies, “whether provided for

⁶⁷⁵ See *SCM Agreement* Art. 1.1.

⁶⁷⁶ *US – FSC* *supra* note 419 at 139.

⁶⁷⁷ *Korea – Commercial Vessels* *supra* note 543 at 7.424-425.

⁶⁷⁸ *US – FSC* *supra* note 354 at para. 7.103

agricultural or other products, confer upon the recipient the obvious benefit of reduced tax liability ... and therefore ... the FSC measure involves a ‘subsidy’ under the *Agreement on Agriculture*.”⁶⁷⁹

The conclusion is that the *SCM Agreement*’s definition of a subsidy can be applied to agricultural subsidies. The three elements required in the *SCM Agreement* to identify a subsidy can be found in agricultural subsidies as well: a) financial contribution, b) an action by a government or a public body and c) a benefit. Even though not all agricultural subsidies are related to direct financial aid, as the *US – FSC* case demonstrated, the *SCM Agreement* does not exclude other kinds of subsidies. However, there is not *a priori* conclusion that all agricultural subsidies can be automatically included in the definition by the *SCM Agreement*. There must be a case-by-case analysis, especially since governments are always innovating new ways to subsidize, because it is part of their state function. Legislative modifications do not happen at the same pace as new forms of subsidies emerge.

Regarding export subsidies, the AB in *US – FSC* analyzed whether “export subsidies” under AoA Art. 1(e) could be considered “contingent upon export performance” under the *SCM Agreement*. The AB saw no reason to not consider that the *AoA* requirement of “contingent upon export performance” was the same as the requirement in the *SCM Agreement*. According to the AB, the two Agreements used “precisely the same words to define ‘export subsidies,’” and the differences in the export subsidies’ discipline in the *AoA* and the *SCM Agreement* did not affect the “common substantive requirement relating to export contingency.” That was the reason why it reached the conclusion the interpretation of export subsidies set forth in the *SCM Agreement* could also be applied to the *AoA*.⁶⁸⁰

⁶⁷⁹ *US – FSC supra* note 419 at para. 140

⁶⁸⁰ *US – FSC* 419 at para. 141.

Therefore, agricultural domestic and export subsidies can be considered as support measures for *SCM Agreement* purposes, because they involve a direct or indirect financial contribution in the sense of Art. 1.1(a)(1), even though a case-by-case analysis is required. The other requirement for the challengeability of subsidies under the *SCM Agreement* is specificity. The next section will examine whether agricultural subsidies can be considered as specific under the *SCM Agreement*.

III.4.1.2 Specificity under the *SCM Agreement*

Another requirement of the *SCM Agreement* for the challengeability of subsidies under Part II, III or V is specificity (*SCM Agreement* Art. 1.2 and Art. 2). A subsidy has to be specific in order to be challengeable. Agricultural subsidies not only can be considered as subsidies according to the criteria established by the *SCM Agreement*, but they can also be specific according to the same agreement.

SCM Agreement Art. 2.1 (c) states that the granting authority has, in order to determine whether a subsidy is specific, to explicitly limit subsidization to a specific enterprise or industry or group of enterprises or industries⁶⁸¹ or to certain enterprises.⁶⁸² In *US – Upland Cotton*, the panel considered the *SCM Agreement* concepts of “industry” and “industries” and concluded that the concept was related to the type of products produced and to producers.⁶⁸³ The panel also stated its determination depended on several factors and had to be determined according to an analysis of each case. It then went further and held that the concept of specificity in *SCM*

⁶⁸¹ *SCM Agreement* Art. 2.1

⁶⁸² *SCM Agreement* Art. 2.1 (a).

⁶⁸³ See *US – Softwood Lumber IV supra* note 533 at para. 7.120 cited in *US – Upland Cotton supra* note 330 at para. 7.1142.

Agreement Art. 2 applies to all goods and must be considered according to the agreement as a whole.⁶⁸⁴ The panel determined the concept of “industries” can be a certain number of producers or even products which broaden the concept and made possible its application to agricultural subsidies given to a product or to producers that grow that product be specific under the *SCM Agreement*. The panel also remembered that *SCM Agreement* is applied to “all goods”, therefore, the concept of specificity cannot excessively narrow this *SCM Agreement* broad application.

SCM Agreement Art. 2.1 (a) and (b) define *de jure* subsidies that are given to certain enterprises under clear conditions established by specific legislation if eligibility is not automatic and such criteria and conditions are not strictly adhered to. Its amount is determined by law, regulation or other official document. *De facto* subsidies,⁶⁸⁵ as seen in Part II of this study, are subsidies that have appearance of non-specificity but are in fact specific because of certain conditions, which are: the “...use of a subsidy program by a limited number of certain enterprises, predominant use by certain enterprises, the granting of disproportionately large amounts of subsidy to certain enterprises, and the manner in which discretion has been exercised by the granting authority in the decision to grant a subsidy”. In this regard, a footnote of the *SCM Agreement*⁶⁸⁶ states information on the frequency with which applications for a subsidy are refused or approved and the reasons for such decision shall be considered.

De facto subsidies make possible that a broader range of support measures be considered specific because it includes the discretion of granting authority and the volume of subsidies as relevant factors to be considered for determination of specificity. For this reason the *US* –

⁶⁸⁴ *Ibid.* at para. 7.1144.

⁶⁸⁵ *SCM Agreement* Art. 2.1(c).

⁶⁸⁶ *SCM Agreement* Article. 2.1 (c), n. 3.

Upland Cotton held that the words of *SCM Agreement* Art. 2.1 determine specificity is a general concept not susceptible to rigid quantitative definition.⁶⁸⁷

The panel's analysis went further and determined that agricultural subsidies given "to a small proportion of industries, such as those producing one or two individual United States' products would be limited and 'thus' specific."⁶⁸⁸ It also determined four types of domestic agricultural subsidies were specific because, even though were not widely available in respect to all agricultural production, they were given to a restricted number of agricultural products.⁶⁸⁹ It concluded that the fact that some producers produce different commodities does not hinder the determination of apparent specificity for their products.⁶⁹⁰

All prohibited subsidies under *SCM Agreement* Part II are deemed to be specific. *SCM Agreement* Article 2.3 states "any subsidy falling under the provisions of Article 3 shall be deemed to be specific". In turn, *SCM Agreement* Art. 3 prohibits two sorts of subsidies: those contingent upon export performance and those contingent upon the use of domestic over imported goods. Green box measures, for example, might well belong to those subsidies contingent upon use of domestic over imported goods *SCM Agreement* 3.1 (b). In this case, they would be deemed specific and could be challengeable.

⁶⁸⁷ *US – Upland Cotton supra* note 330 at para. 7.1142.

⁶⁸⁸ *Ibid.* at 7.1147.

⁶⁸⁹ The panel decided:

Other measures before us pertain to a restricted number of agricultural products, but are not widely or generally available in respect of all agricultural production, let alone the entire universe of United States production of goods. These measures include the marketing loan programme payments. They also include the measures available in respect of upland cotton as part of a restricted basket of agricultural commodities. These are the four types of domestic support which permit production flexibility (PFC, MLA, DP and CCP payments) that were or are provided in respect of certain agricultural production in a base period which satisfies certain eligibility criteria. These criteria have the effect of limiting eligibility to a subset of basic agricultural products, including upland cotton or certain other programme crops. We therefore find that these subsidies are "specific" within the meaning of Article 2. *Ibid.* at 7.1148.

⁶⁹⁰ "The fact that some of the subsidies go to farmers who may produce different commodities, or, in theory, may not produce a given commodity does not mean, by some process of reverse reasoning, that the specificity that is apparent from the face of the grant instrument no longer exists". *Ibid.*

In *US – Upland Cotton*, the panel determined that because *SCM Agreement* Art.2.3 established that all prohibited subsidies are specific, Step 2 payments and other similar types of subsidies that were deemed prohibited under Art. 3.1(a) and (b) by the panel were declared specific within the meaning of *SCM Agreement* Art. 2.3.⁶⁹¹ The panel adopted a very broad concept of specificity and determined most of the agricultural subsidies challenged under the *SCM Agreement* in the dispute were specific either by virtue of *SCM Agreement* Art. 2.1 (c) (*de facto* specificity) or Art. 2.3 (prohibited subsidies are deemed to be specific).

Even though specificity of agricultural subsidies can only be determined on a case-by-case basis, it was seen that specificity requirement is not an obstacle for challengeability of agricultural subsidies, even if it is given to more than one crop or to different producers that grow different crops.

III.4.1.3 The Challengeability of Agricultural Subsidies under the *SCM Agreement* Part II

SCM Agreement Part II Art. 3 establishes that “except as provided in the *AoA*,” certain subsidies shall be prohibited. This statement was interpreted for several years as being a free ride for agricultural subsidization. However it only recognizes that there is a specific *Agreement on Agriculture* that must first be analyzed and respected for the purposes of challengeability.

The rationale is that, during the peace years, several subsidies linked to export subsidies were allowed if given according to and under the limits of the *AoA* schedules. If *SCM Agreement* Art. 3.1 had also clearly prohibited any form of agricultural subsidy, there would be a conflict between *SCM Agreement* Art. 3, which prohibits export subsidies, and *AoA* Art. 9, which

⁶⁹¹ *Ibid.* at 7.1153

authorizes determined types of agricultural export subsidies under certain circumstances. In this case, Art. 9 would prevail, because it is the most specific provision.

The *raison d'être* of the statement “except as provided in the *Agreement on Agriculture*” was exactly that of accommodating the general prohibition of *SCM Agreement* Art. 3. to the exception of *AoA* Art. 9, which authorizes agricultural export subsidization within determined limits. One could state that, if this was the intention of the negotiators, then *SCM Agreement* Art. 3 had to include the same statement as in Art. 5, which establishes that “[t]his article does not apply to subsidies maintained on agricultural products as provided in Article 13 of the *Agreement on Agriculture*.”

There is an important difference in the nature of these two provisions that must be considered. *SCM Agreement* Art. 3 absolutely prohibits export subsidization, and Art. 5 does not institute a flat prohibition. It establishes some limits for the actionability of subsidies that cause adverse effects. Subsidies regulated under *SCM Agreement* Art. 3 are prohibited *a priori*, but subsidies regulated under Art. 5 have to go through a process of verification to determine if they cause injury, nullification or impairment or serious prejudice in order to be prohibited.

Therefore, the phrase “except as provided in the *Agreement on Agriculture*” means that the *a priori* *SCM Agreement* prohibition of export subsidies has to be considered in conjunction with the *AoA* in order to be applied to agricultural export subsidies. *SCM Agreement* Art. 5 does not have a prohibition *a priori*, and for this reason, instead of stating “except as provided in the *Agreement on Agriculture*,” it states that the article “does not apply to subsidies maintained on agricultural products as provided in Article 13 of the *Agreement on Agriculture*.”

Since there is no *a priori* prohibition, there is no need to clarify that the *AoA* has to be considered in conjunction with whatever regards the challengeability of agricultural subsidies.

This application of the *AoA* and the *SCM Agreement* in conjunction regarding the challengeability of agricultural subsidies is presumed, because of all the principles and the *GATT 1994* and WTO cases already studied in this research and all the cross-references in these two agreements.

However, because *SCM Agreement* provisions do not have an expiration date and *AoA* Art. 13 establishes a period of time during which the challengeability of agricultural subsidies would be limited, it should be clarified that, until the expiration of the Peace Clause, agricultural subsidies were exempt from challenges under *SCM Agreement* Arts. 5 and 6. Each article makes exactly the same observation, stating that it “does not apply to subsidies maintained on agricultural products as provided in Article 13 of the *Agreement on Agriculture*.”

One could state that, if agricultural export subsidies were prohibited, they would not have been authorized under certain circumstances and in accordance with *AoA* schedules. The decision in *US – Upland Cotton*, presented below, responds to this observation.

The panel analyzed challengeability of agricultural export subsidies under *SCM Agreement* Art. 3 and remembered that according to *AoA* Art. 21.1, the *AoA* takes precedence in case of conflict. The panel stated there would be a conflict if there was an explicit exemption from the disciplines in *SCM Agreement* Art. 3.1 in the text of the *AoA*. Another possible conflict would be if it was not possible for a Member to comply with disciplines of *AoA* and with *SCM Agreement* Art. 3 at the same time or if there was an explicit authorization in the *AoA* that would go against the prohibition of *SCM Agreement* Art. 3.⁶⁹² The panel then concluded that the *AoA*

⁶⁹² *US – Upland Cotton supra* note 330 at para. 7.1038.

and Article 3 of the *SCM Agreement* did not present any conflict,⁶⁹³ and that *AoA* Art. 9.1(a) did not conflict and could be applied together with *SCM Agreement* Art. 3.1(a).⁶⁹⁴

It was seen in section III.5.3.2 of this study that the prohibition provisions of *SCM Agreement* Art. 3.1 do not conflict with the exemption provisions of *AoA* Art. 9. Therefore, there is no conflict between these two provisions and they can be applied together as already analyzed herein. Therefore upon the expiry of the Peace Clause, any agricultural subsidy contingent upon exports can be challenged under *SCM Agreement* Article 3.1(a).

III.4.1.4 The Actionability of Agricultural Subsidies under *SCM Agreement* Part III

According to *SCM Agreement* Part III (actionable subsidies), Article 5, no Member should cause adverse effects to another Member through the use of subsidies. The Article distinguishes between three types of adverse effects that can be challenged. The first occurs when a WTO Member injures the domestic industry of another Member. Footnote 11 of the *SCM Agreement* states that the term injury is used in the same sense as it is used in Part V of the *SCM Agreement*.

This first type of adverse effects can be challenged, either through countervailing actions, or under the WTO dispute settlement system. However, DSB actions and countervailing cases are not mutually exclusive. Both jurisdictions can be used at the same time according to *SCM Agreement* Article 10, footnote 35. Although “with regard to the effects of a particular subsidy in the domestic market of the importing Member, only one form of relief (either a countervailing duty, if the requirements of Part V are met, or a countermeasure under Articles 4 or 7) shall be

⁶⁹³ *Ibid.* at 7.1040.

⁶⁹⁴ *Ibid.* at 7.759.

available.” It means countervailing duties cannot be applied together with the procedures of *SCM Agreement* Art. 4 or 7. Only one *SCM Agreement* remedy can be used regarding actionability of subsidies in the national market.

The second type of adverse effect is nullification or impairment of benefits accruing directly or indirectly to other Members under *GATT 1994*, in particular the benefits of concessions bound under Article II of the *GATT 1994*.⁶⁹⁵ Footnote 12 states the term “nullification or impairment” is used in the same sense it was used in *GATT 1994*. *GATT 1994* Art. XXIII established concessions can be suspended in the following cases where: any Member has any benefit being nullified or impaired; failure of another contracting party to carry out its obligations under the *GATT 1994*; violation of any provision of *GATT 1994*; the application of any measure, even if it does not conflict with *GATT 1994*; and the existence of any other situation.⁶⁹⁶

Under *GATT 1994*, nullification and impairment is a broad provision that can give legal basis to challenges even if the challenged measures do not violate any agreement (non-violation cases). In the same way, this provision under the *SCM Agreement* Art. 5 protects not only rights established in the WTO agreements, but also mere expectation of rights.

The third type of adverse effect is the aforementioned serious prejudice, which has the same meaning as in paragraph 1 of Art. XVI of the *GATT 1994* and includes threat of serious prejudice. *SCM Agreement* Art. 6.3 states that:

“serious prejudice may arise in any of the following cases: (a) to ‘displace or impede the imports of a like product of another Member into the market of the subsidizing Member’; (b) to ‘displace or impede the exports of a like product of another Member from a third country market’; (c) significant price undercutting suppression, depression or lost sales, in the same market by the subsidized product as compared with the price of a like product of another Member in the

⁶⁹⁵ *SCM Agreement*, Article 5 (b).

⁶⁹⁶ *GATT 1994* Art. XXIII:1(a)(b) and (c).

same market'; (d) 'an increase in the world market share of the subsidizing Member in a particular subsidized primary product or commodity', ... as compared to the average share it had during the previous period of three years and with the increase following a consistent trend over a period when subsidies have been granted."⁶⁹⁷

Item d is particularly important, because it replaced the "more than an equitable share" concept of TRSC Art. 10.1 and *GATT 1994* Art. XVI. As was seen in Part II of this study, the *SCM Agreement* raises the threshold to challenge agricultural subsidies because it includes displacement as another requirement for the challengeability of agricultural subsidies.

In *United States – Subsidies on Upland Cotton – Recourse to Article 21.5 of the DSU by Brazil [US – Upland Cotton (Article 21.5 – Brazil)]* the panel stated that the situations listed in Article 6.3(a)-(d) constituted serious prejudice, and therefore, a "finding of significant price suppression under Article 6.3(c) of the *SCM Agreement* is sufficient basis for a finding of serious prejudice within the meaning of Article 5(c) of the *SCM Agreement*."⁶⁹⁸ In *Korea – Commercial Vessels* the panel stated that the situation listed in Article 6.3(a)-(d) "in themselves constitute serious prejudice."⁶⁹⁹ In these decisions, the panels clearly stated that, if serious prejudice could be proved under Article 6.3, it could be proved under Art. 5(c) as well, because the threshold in Art. 6.3 is higher than in Art. 5(c). Art. 6.2 establishes that serious prejudice will not be attributed if the subsidizing Member proves that its subsidy has not resulted in any of the effects enumerated in *SCM Agreement* Art. 6.3.

Therefore, under the current *SCM Agreement* rules, serious prejudice only can be found if the subsidy results in displacement, price undercutting or an increase in the world market share. *SCM Agreement* Footnote 13 establishes that the term "serious prejudice" used in Art. 5(c) has

⁶⁹⁷ *SCM Agreement* Article 6.3

⁶⁹⁸ Panel Report, *United States – Subsidies on Upland Cotton. Recourse by Article 21.5 of DSU* (2007) WTO Doc. WT/DS267/RW and Corr.1, adopted 20 June 2008, at para. 10.225 as modified by Appellate Body Report WT/DS267/AB/RW [*US – Upland Cotton (Article 21.5 – Brazil)*].

⁶⁹⁹ *Korea – Commercial Vessels supra* note 542 at paras. 7.581-587.

the same sense as in *GATT 1994* Art. XVI. In turn, the *GATT 1994* did not precisely describe the concept of serious prejudice, and therefore, it could be demonstrated without proving displacement, price suppression or an increase in the market share if it did not refer to an export subsidy. Therefore, the concept of serious prejudice in the *SCM Agreement* has the same sense as in *GATT 1994*, but it cannot be proved without at least one of the consequences established in *SCM Agreement* Art. 6.3.

In *US – Upland Cotton (Article 21.5 – Brazil)*, the Appellate Body quoted the original panel, which had identified three steps to be taken to define the concept of price suppression established in *SCM Agreement* 6.3(c): “(i) there was price suppression in the world market for upland cotton, (ii) this price suppression was significant and (iii) a causal relationship existed between this significant price suppression and certain price-contingent subsidies.”⁷⁰⁰ Based on this approach, the panel held that certain price-contingent subsidies (marketing loan payments, counter-cyclical payments, Step 2 payments and market loss assistance payments) collectively caused significant price suppression in the world market for upland cotton and, consequently, serious prejudice to the interests of Brazil.⁷⁰¹

As was seen, *SCM Agreement* Art. 5 established that this provision did not apply to subsidies maintained on agricultural products because of the shield of the Peace Clause. Art. 6 has the same provision in paragraph 9, stating that it does not apply to agricultural subsidies as provided for in AoA Art 13. This is clear evidence that, since the expiry of the Peace Clause, *SCM Agreement* Part III applies to agricultural subsidies. Besides, if agricultural subsidies can be subject to *SCM Agreement* Art. 3 in Part II—a substantively stringent provision that prohibits certain types of subsidies—there is no reason that the less stringent and procedural provision of

⁷⁰⁰ *US – Upland Cotton supra* note 14 at paras. 7.1275-7.1363.

⁷⁰¹ *US – Upland Cotton (Article 21.5 – Brazil) supra* note 698 at para. 10.51.

Art. 5 should not be applied to agricultural subsidies. The mention of the Peace Clause in Arts. 5 and 6 only corroborates this.

However, the actionability of agricultural subsidies under *SCM Agreement* Part III is not automatic. They have to cause one of the three types of adverse effects: injury, nullification or impairment or serious prejudice. If it is injury, it has to be proved under all the detailed requirements and procedures of *SCM Agreement* Art. 15, because footnote 11 says that, in *SCM Agreement* Art. 5, an injury has the same sense as in *SCM Agreement* Part V, which regulates countervailing duties.

A mere expectation of a right can also be challenged under *GATT 1994* Art. XXIII 1(b) (non-violation claim), but the complainant must demonstrate a) the application of a measure by a WTO Member, b) a benefit accruing under a relevant agreement, and (c) nullification or impairment of the benefit as the result of the application of the measure.

Also, reasonable expectation must exist, which is whether or not it would be reasonable to expect that the benefit under an existing concession or mere expectation of right would be impaired by the measures challenged. It should be pointed out that a non-violation claim can be raised when the challenged measure is taken outside of the WTO agreement but impairs commitments or expectations arising within the WTO agreement.⁷⁰²

If it is serious prejudice, even though the sense is the same as used in the *GATT 1994*, one of the effects—displacement, price undercutting or increase in market share, according to the parameters and requirements of *SCM Agreement* Art. 6.4 and 6.5—established under *SCM Agreement* Art. 6.3 for a successful claim must exist. Agricultural subsidies can now be challenged under *SCM Agreement* Part III after the expiry of the Peace Clause, but it must be

⁷⁰² Panel Report, *Korea – Measures Affecting Government Procurement* (2000), WTO Doc. WT/DS163/R, at para 7.93 adopted 19 June 2000, DSR 2000:VIII, 3541 [*Korea – Procurement*].

proved that the challenged agricultural subsidy caused one of these adverse effects examined above.

The most difficult type of adverse effect to be proved is an allegation of serious prejudice under *SCM Agreement* 5(c) and 6.3, because of the link that the *SCM Agreement* establishes between this concept and either price suppression, displacement or increase in market share. The requirements to prove price suppression have already been analyzed in this section. The effects on market share, a concept originating in *GATT 1994* Art. XVI, and displacement, which was already present in the TRSC, will be analyzed next.

III.4.1.4.1 The Effect on World Market Share and Displacement

The concept of displacement as a requirement for the challengeability of subsidies did not exist in the *GATT 1947*, only the concept of world market share for the challengeability of agricultural subsidies with an impact on exports, whose origins lay in the *Havana Charter*.⁷⁰³ Under this simpler and less complex requirement for challengeability, agricultural subsidies were condemned by several *GATT 1947* cases that limited the application of agricultural distortive support measures.⁷⁰⁴ However, there is evidence that condemnation became more difficult over the years, especially after the TRSC linked the concept of displacement with proving that a country was getting more than an equitable share of the market. *EC – Sugar Exports (Australia)* and *EC – Sugar Exports (Brazil)* decided in 1980 and 1981, respectively, were the first cases after the Tokyo Round (1973-1979) that implemented TRSC Art. 10:2, which determined that

⁷⁰³ The *Havana Charter* *supra* note 67. See section I.2.1.3 of this study in Part I.

⁷⁰⁴ *France – Wheat Exports* *supra* note 64. *EC – Sugar Exports (Brazil)* *supra* note 54, *EC – Sugar Exports (Brazil)* *supra* note 54, *EEC – Wheat Flour Subsidies* *supra* note 54, *EEC – Pasta Subsidies* *supra* note 163, *EEC – Oilseeds I* *supra* note 54, *EEC – Canned Fruits* *supra* note 228 and *US – Dairy* *supra* note 260.

displacement was a requirement for the challengeability of agricultural subsidies. The consequence was that, even though the panel found that there was a change in the relative positions of Brazil and the EC in the sugar market caused by European subsidies, it could not provide clear and general evidence that Brazilian exports on sugar had been directly displaced by subsidized exports of EC sugar in specific markets.⁷⁰⁵

This panel substantively condemned the agricultural subsidies for sugar given by the EC, because it determined that serious prejudice had been caused to other exporters, even though displacement could not be proved. This condemnation of serious prejudice would not have been possible had it been made after the implementation of the *SCM Agreement* in the WTO in 1995, because currently, displacement is a requirement for the determination of serious prejudice. Since the decision in the *EC – Sugar Exports* cases, panels had substantively condemned agricultural subsidization but with no determination that they had caused the subsidizing country to have more than an equitable share of world export trade in that product.

In *EEC – Wheat Flour Subsidies*, the panel stated that EEC export refunds for wheat were subsidies and that it could identify artificial levels of trade in the wheat flour market. However, the panel could not decide on whether European illegal subsidization did not conform to TRSC Art. 10, which regulated displacement, because “market displacement in the sense of Article 10:2(a) was not evident in the seventeen markets examined by the Panel.”⁷⁰⁶

In *EEC – Pasta Subsidies*, the panel held that EC subsidies on exports of pasta products were granted in a manner inconsistent with TRSC Art. 9⁷⁰⁷ and identified strong evidence that the EC had gained more than an equitable share because of its subsidies for pasta. However, it did not clearly state that European subsidies for pasta had given to the EC more than an equitable

⁷⁰⁵ *EC – Sugar Exports (Brazil)* *supra* note 54 at para. 4.15.

⁷⁰⁶ *EEC – Wheat Flour Subsidies* *supra* note 54 at 36.

⁷⁰⁷ *Ibid.* at 10 para. 4.4

share of the world export trade. In both decisions, the panels were clear about the illegality of the given export subsidies but did not condemn them under the provision of *GATT 1994* Art. XVI.

The condemnation of agricultural subsidies under *GATT 1947* Art. XVI is proof that the problem was not in the concept of “more than an equitable share” but in its association with displacement in the TRSC. As was seen, this Code was not implemented by all *GATT* contracting parties and brought in several procedural innovations regarding the challengeability of subsidies, especially regarding countervailing duties. The same could not be said in terms of substantive rules, because they significantly increased the thresholds for the challengeability of agricultural subsidies.

Even in *US – Upland Cotton*, which was a landmark case in the condemnation of agricultural subsidization, the panel declined to rule on the *GATT 1994* Art. XVI claim.⁷⁰⁸ It could be said that, after the implementation of the *AoA* and the *SCM Agreement*, the condemnation of subsidization under *GATT 1947* Art. XVI is no longer relevant. It might be true, but it does not invalidate the conclusion that, during the *GATT* years, there was a rationale to limit agricultural subsidization, as verified in the first part of this research. In footnote 521 of the *US – Upland Cotton* case, the Appellate Body observed that it was difficult to ascertain whether imports or exports were displaced or impeded under *SCM Agreement* paragraphs (a) or (b) of Article 6.3.⁷⁰⁹ That might be one of the reasons why the panel and the AB did not work much with the concept of displacement in order to determine that American cotton subsidies were

⁷⁰⁸ The AB “decline[d] to rule on Brazil’s conditional request for the Appellate Body to find that the price-contingent subsidies cause the United States to have “more than an equitable share of world export trade” in upland cotton, in violation of the second sentence of Article XVI:3 of the *GATT 1994*.” *US – Upland Cotton supra* note 14 at 394.

⁷⁰⁹ *US – Upland Cotton supra* note 8 at n. 521.

illegal under the *SCM Agreement*. Even though the panel declined to rule on the expression, it gave some hints for future cases, stating:

As regards the interpretation of the term “world market share” in Article 6.3(d) of the *SCM Agreement*, Brazil first draws support from the text of that provision. Article 6.3(d) does not specify whether “world market share” refers to world market share of production or world market share of something else. However, the use of the word “trade” in footnote 17 to Article 6.3(d) suggests that Article 6.3(d) is directed towards a Member’s share of world trade in a product, which requires a focus on *exports* rather than *production*.⁷¹⁰

Regarding the actionability of agricultural subsidies under *SCM Agreement* Art. 6.3(d), which replaced the “more than equitable” *GATT 1994* provision, two relevant conclusions must be arrived at. The first is that Art. 6.3(d) refers to agricultural products. Footnote 17 of the article states that “unless other multilaterally agreed specific rules apply to the trade in the product or commodity in question.” The purposeful use of the word “commodity” in the text proves that the article was meant to apply to agricultural products; otherwise, the mention would not make sense.

Taking into account that *SCM Agreement* Art. 6.3 is an elaboration on *GATT 1947* Article XVI:3 and *GATT 1947* Ad Art. XVI Section B 2 states that “a primary product is understood to be any product of farm, forest or fishery, or any mineral, in its natural form or which has undergone such processing as is customary required to prepare it for marketing in substantial volume in international trade.” There is no doubt that agricultural products are referred to as primary products under the *GATT 1994* and the *SCM Agreement*. The second conclusion is that a primary product is an agricultural product under the *SCM Agreement* and *GATT 1994*, which corroborates the fact that not only *SCM Agreement* Art. 6.3(d) but also all provisions of *SCM Agreement* Part III can be read together with the *AOA*.

⁷¹⁰ *Ibid.* at para. 136.

III.4.1.5 The Challengeability of Agricultural Subsidies under *SCM Agreement Part V*

It should be clarified that countervailing duties are domestic trade remedies and their regulation under the WTO provides for a different obligation. In this case, the WTO agreements only give a legal guidance for the national application of these remedies on the country of the imported goods.”⁷¹¹ However the exporting Member still can bring a case under the WTO dispute settlement system about the countervailing investigation or duty complaining that the importing Member has violated its obligations under the WTO.⁷¹²

SCM Agreement Part V regulates countervailing measures. Art. 10 states that Members shall take all necessary steps to guarantee countervailing duties imposed in the territory of an importer have to be in accordance with *GATT 1994* Art. VI, the *SCM Agreement* and the *AoA*. The first paragraph of Part V states that the regulation is applied to agricultural subsidies. During the peace years, green box subsidies were non-challengeable for the purposes of countervailing duties. Amber, blue box and export measures were exempted from countervailing duties unless a determination of injury was made and due restraint⁷¹³ had to be exercised. Now that the Peace Clause has expired, any agricultural subsidy can be countervailed under *GATT 1994* Art. VI and *SCM Agreement Part V* by virtue of by virtue of *SCM Agreement Art. 10*.

⁷¹¹ See *infra* note 750

⁷¹² The use of the term challengeability does not include countervailing duties. In only include potential WTO challenges.

⁷¹³ The concept of due restraint was analyzed in *Mexico – Olive Oil* that defined it as a “proper, regular and reasonable demonstration of self-control, caution, prudence and reserve.” According to the panel, Mexico imposed countervailing measures but with due restraint because the country acted with “self-control”, there was no “material retardation” and initiation with no consultations did not mean lack of due restraint. *Mexico – Olive Oil supra* note 320 at paras. 7.70-7.79.

The requirements for countervailability for agricultural subsidies are specificity and causation of material injury or threat of causation of material injury to a WTO Member's domestic industry. The requirements are the same as for non-agricultural products.

Article 15.1 of the *SCM Agreement* states that, for a determination of injury⁷¹⁴ according to purposes of Article VI of *GATT 1994* (countervailing duties and anti-dumping), a) the volume of subsidized imports and the effect of such imports on prices in domestic market for like products and b) the consequent impact of those imports on domestic producers must be examined. It is relevant to mention that not only subsidies but also external factors can have an influence on a determination of injury. Because subsidization is one factor that might cause injury, other external factors also have to be identified as it will be analyzed below.

The criteria to evaluate the first item (examination of the volume of subsidized imports and its consequent impacts on prices in the importing domestic market) are the same for non-agricultural and agricultural products. There must be an examination by the investigating authority of factors such as whether a significant increase in subsidized imports in absolute or relative terms occurred; whether there is price undercutting caused by the subsidized import, as compared with the price of a like product; and whether such imports depressed prices to a degree that prevented price increases.⁷¹⁵

SCM Agreement Art. 15.4 requires one more examination for the second item for a determination of injury (impact of imports on domestic producers) for agricultural products. It states that the verification of the impact of subsidized imports on the domestic industry shall

⁷¹⁴ The term injury used in *SCM Agreement* Part V, is the same used in Part II and III. "Under this Agreement the term "injury" shall, unless otherwise specified, be taken to mean material injury to a domestic, threat of material injury to a domestic industry or material retardation of the establishment of such an industry and shall be interpreted in accordance with the provisions of this Article." *SCM Agreement* n. 46.

⁷¹⁵ *SCM Agreement* gives the concept of a like product. "Throughout this Agreement the term "like product" ("produit similaire") shall be interpreted to mean a product which is identical, i.e. alike in all respects to the product under consideration, or in the absence of such a product, another product which, although not alike in all respects, has characteristics closely resembling those of the product under consideration."

include (for agricultural and non-agricultural products) an “evaluation of all relevant economic factors and indices having a bearing on the state of the industry.”⁷¹⁶ The list of these economic factors is not exhaustive and includes: actual and potential decline in output, sales, market share, profits, productivity, return on investments, or utilization of capacity; factors affecting domestic prices; actual and potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investments. For agricultural products, the article stated one more condition for a verification of the impact of subsidized imports on the domestic industry: an examination of whether there has been an increased burden on government support programmes.

This additional criteria established in the *SCM Agreement* Art. 15.4 leads to two conclusions. First, it proves countervailing duties were meant to apply to agricultural products. Therefore, after the expiry of the Peace Clause, there is no more restriction for challengeability of agricultural subsidies under *SCM Agreement* Part V. Secondly, the requirements for a determination of injury for agricultural products are higher than for non-agricultural products.

The list already contemplates several economic factors regarding impacts of subsidized imports on the domestic industry. The additional requirement for agriculture includes an evaluation regarding consequences on domestic government and not regarding impacts of subsidies on domestic industry that is the goal of the list. An evaluation of whether there is an increased burden on government support programs not related to the domestic industry of the importing country might require an examination of several other different economic and non-economic factors.

As has been seen, the *SCM Agreement* considerably increased the thresholds for countervailability with the addition of requirement for the evaluation of several economic factors

⁷¹⁶ *SCM Agreement* Art. 15.4.

for an injury determination. As was determined above, the condition for the countervailability of agricultural subsidies became even higher than for non-agricultural subsidies.

According to the *US – Upland Cotton* panel, external factors other than subsidization have to be separated and identified for a determination of injury. The AB already decided that “a causal link ‘between increased imports of the product concerned and serious injury or threat thereof’ “involves a genuine and substantial relationship of cause and effect between these two elements,” and it has also required non-attribution of effects caused by other factors.⁷¹⁷

The AB stated that not only subsidization and injury must exist, but also a causal link between these two factors is needed for a successful challenge to agricultural subsidies under *SCM Agreement* Part V. Therefore, determination of the countervailability of agricultural subsidies under *SCM Agreement* Part V depends upon a) subsidies given by an exporting Member; b) a determination of injury based on economic impact not only on the importing domestic industry, but also on the importing government and c) a causal link between these two factors.

As a result, green box subsidies have a smaller probability of being countervailed than do export, amber or blue box subsidies, because they are not supposed to be distortive. At any rate, if export, amber, blue and even green box subsidies cause injury and a causal link can be proved, they can be countervailed under *SCM Agreement* Part V after the expiry of the Peace Clause.

III.4.2 The Challengeability of Agricultural Subsidies under the *GATT 1994*

The Peace Clause hindered the challengeability of agricultural subsidies under two *GATT 1994* articles: XVI and XXIII 1(b) (via Art. II), which represented actions based on non-violation

⁷¹⁷ *US – Upland Cotton* *supra* note 14 at para. 431 [footnotes omitted].

nullification or impairment of the benefits of tariff concessions accruing to another Member. During the Peace Clause years, green box subsidies were completely exempt from claims based on *GATT 1994* Art. XVI and non-violation claims under Art. XXIII 1(b). Amber and blue box measures were exempt from claims based on *GATT 1994* Art. XVI and non-violation claims if such measures did not grant subsidies to a specific product in excess of the levels decided during the 1992 marketing year. Export subsidies were completely exempt from actions based on *GATT 1994* Art. XVI. *GATT 1994* Art. XVI established that, for subsidies that caused serious prejudice to the interests of any other Member, there should be discussions with the other Member to examine the possibility of limiting the subsidization. The same article established that parties should seek to avoid giving export subsidies that would give them more than an equitable share of the world export trade in a specific product. It should be noted that the concept of limiting domestic subsidization that cause serious prejudice established by Art. XVI is currently also included in the *AoA*, especially Art. 6 and Annex II, and the *SCM Agreement*, especially Part I, III and V. The same could be said about the part of *GATT 1994* Art. XVI that aims at limiting export subsidies, whose concept is also currently included in the *AoA*, especially Arts. 8, 9, 10 and 11, and *SCM Agreement*, especially Part I, II and V.

SCM Agreement and *GATT 1994* Arts. XVI and XXIII 1(b) can be considered to have a *residual character* because the challengeability of agricultural subsidies has to currently meet higher thresholds under the *AoA* and especially under the *SCM Agreement*. For this reason, currently, these two provisions are rarely used to challenge agricultural subsidies.

As was previously stated, a non-violation claim under *GATT 1994* Art. XXIII 1(b) can be based on a mere expectation of a right. The right is normally a reciprocal tariff concession negotiated among Members under *GATT 1994* Article II. A Member can bring a non-violation

complaint when a hypothetical benefit of tariff concession is violated by the practice of a subsidy. DSU Art. 26.1 establishes some rules for challenges under *GATT 1994* Art. XXIII. It establishes that, if a Member brings a claim under *GATT 1994* Art. XXIII 1(b), the panel has to analyze whether the challenged measure conflicts with a covered agreement and nullify or impair any benefit given to the complainant. Verification is also required of whether any goal of the agreement is being hindered as a result of the application of the challenged measure by the respondent. If the challenged measure does not conflict with any agreement, the procedures have to be guided by some DSU rules. The first is that the complainant has to present a detailed justification regarding the challenged measure that does not conflict with any agreement. The DSU establishes that, if the challenged measure nullifies or impairs any benefit given to the complainant but does not violate any agreement, the respondent has no obligation to withdraw the measure. However, the panel or the AB has to recommend a mutually satisfactory adjustment between the parties.

The parties can resort to arbitration procedures of DSU Art. 21 to not only determine a period of time for implementation of the panel or AB decision but also to rule on the level of benefits that have been impaired or nullified. Also, suggestions for a satisfactory agreement can be presented, even though such suggestions will not be binding upon the parties. Compensation can be part of a satisfactory agreement between the parties.⁷¹⁸

The DSU established that the panel or AB decision on a *GATT 1994* Art. XXIII 1(b) complaint must be limited to the matter of the case, which is the impaired or nullified benefit or an obstacle to the attainment of any objective of any WTO agreement. After the report is circulated to WTO Members, the implementation and surveillance of the rulings have to follow

⁷¹⁸ DSU Art. 26:1 (a)-(d).

the Decision of 12 April 1989.⁷¹⁹ This means that, after the circulation of the decision to Members, the DSB does not have to adopt the decision, and the formal DSB procedures for adoption and implementation (DSU Arts. 16.1, 16.4, 17.14, and 21.3) do not have to be observed. Instead, the parties have to negotiate to reach a mutual agreement. The DSB establishes a simpler procedure that, according to the Decision of 12 April 1989, cannot take longer than 15 months, among other rules.⁷²⁰

At any rate, the complainant also has to present a detailed justification of its arguments regarding the challenged measure or agreement. If there is any other matter besides those mentioned above, regulated by DSU Art. 26.2, the panel shall circulate a report to the DSB to address such measures in a separate report.⁷²¹

There were some non-violation cases in *GATT 1994* and WTO history involving domestic subsidies that allegedly impaired or nullified benefits of tariff concessions. As was seen, *Korea – Procurement*⁷²² defined some requirements for a non-violation case. The first requirement was that the complainant must have legitimate expectations that the defending party will make a tariff concession; the second requirement was that the complainant could not have reasonably anticipated the controversial measure at the time the concession was granted; and the last requirement was that the disputed measure must have upset the competitive position of the imported product concerned.

⁷¹⁹ See *supra* note 44.

⁷²⁰ It established that reports shall not be considered for adoption until thirty days after they have been issued to contracting parties; if contracting parties have objections to panel reports, they have to give written reasons to explain their objections at least ten days prior to the meeting where the report will be considered; parties can participate in the consideration of the panel report and it has to be adopted by consensus; the implementation of the recommendations shall be monitored among other regulations. *Ibid.*

⁷²¹ It is interesting to note that the challenged provision can be brought under GATT Art. XXIII, but the procedures for a non-violation claim or for a dispute brought under Art. XXIII 1(c) are regulated by the DSU.

⁷²² *Korea – Procurement supra* note 702.

Therefore, agricultural subsidies can be challenged under *GATT 1994* Art. XXIII 1(b) because: a) it is difficult for an agricultural subsidy to be reasonably anticipated at the moment of the concession, because it depends on national governmental policies; b) it has already been shown that subsidies can harm the competitive position of an imported product; and c) an agricultural subsidy can harm a legitimate expectation of Member when, for example, a tariff concession is given under *GATT 1994* Art. II for one product and the Member heavily subsidizes the same product.

Once these three requirements have been met, agricultural subsidies can be challenged under *GATT 1994* Art. XXIII 1(b). A causal link between the agricultural subsidy that purportedly violated a concession and the nullified or impaired benefit has to be proved. If the complainant is successful in proving that a benefit has been nullified or impaired because of the subsidy, it can suspend the application of a concession or other obligation under any WTO agreement.⁷²³

Therefore, if a WTO agreement is violated, there are fewer benefits to challenging an agricultural subsidy under Art. XXIII 1(b). Furthermore, in order for agricultural subsidies to be challengeable they have to cause adverse effects; otherwise, there is no interest in challengeability. And if they cause adverse effects, they most likely will violate the *SCM Agreement*. At any rate, after the expiry of the Peace Clause, green, blue, amber and export subsidies are no longer exempt from actions based on *GATT 1994* Art. XVI and Art. XXIII 1(b), even though these articles have a *residual character* and are not frequently used. This is why the

⁷²³ *GATT 1994* Article XXIII.2 establishes that "... [i]f the contracting parties consider that the circumstances are serious enough to justify such action, they may authorize a contracting party or parties to suspend the application to any other contracting party or parties of such concessions or other obligations under this Agreement as they determine to be appropriate in the circumstances..."

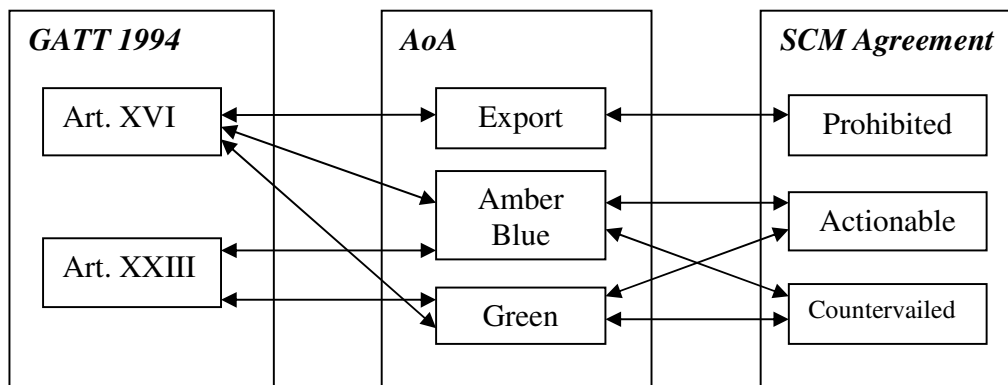
challengeability of agricultural subsidies is more likely to happen under the *SCM Agreement* than under the *GATT 1994*.

After this analysis, it is possible to define the zone of confluence of the challengeability of agricultural subsidies and describe the new boundaries for challengeability upon the expiry of the Peace Clause.

III.5 The New Boundaries for the Challengeability of Agricultural Subsidies upon the Expiry of the Peace Clause

After the expiry of the Peace Clause, there is a zone of confluence of challengeability for agricultural subsidies between the *AoA*, the *SCM Agreement* and also the *GATT 1994*, according to the diagram below. The limits of the zone will be analyzed next.

Diagram 2: Zone of Confluence of the Challengeability of Agricultural Subsidies



The arrow means a relation of challengeability.

There is no more doubt about whether the expiry of the Peace Clause made agricultural subsidies subject to legal challenges under the provisions of the *SCM Agreement*, regardless of whether they are categorized as export subsidies or amber, blue or green box domestic support.

This study concludes that there is no conflict among the WTO agreements that regulate agricultural subsidies, and for this reason, the *SCM Agreement* applies to all agricultural subsidies. This means that, currently, they are all challengeable. However, the new limits for the challengeability of each type of agricultural subsidy have to be clarified.

Even with the new boundaries for challengeability, agricultural subsidies have to have trade-distorting effects in order to be successfully challenged. The expiration of the Peace Clause, however, does mean that government payments to farmers are no longer protected from challenge, simply because they are classified in specific boxes or because they do not exceed pre-determined limits.

This study has shown that the new boundaries for challengeability were determined after the expiry of the Peace Clause. Now, we turn to the fundamental point of defining the new boundaries for the challengeability of each type of agricultural subsidy: green, non-green and export support.

III.5.1 Green Box Subsidies

Green box subsidies are, in theory, the least trade-distortive domestic measures. They conform to *AoA* Art. 6.1 and Annex 2, which includes various categories of government expenditures that are considered to be minimally or non-trade-distorting, because they cannot be characterized as price supports and do not encourage production. Green box subsidies include both the general provision of government services, such as infrastructure and research, and

determined direct payments to farm producers, including payments under environmental and conservation programs.⁷²⁴

Under the Peace Clause, conforming green box subsidies were non-challengeable subsidies for the purposes of countervailing duty measures,⁷²⁵ exempt from actions based on Article XVI of *GATT 1994* and Part III of *SCM Agreement*⁷²⁶ and exempt from actions based on non-violation, nullification or impairment of the benefits of tariff concessions, accruing to another Member under Article II of *GATT 1994*, in the sense of paragraph 1(b) of Article XXIII of *GATT 1994*.⁷²⁷

It must be noted that the *AoA* does not contain any provision dealing specifically with the imposition of countervailing duties. Nor does it suggest that a Member cannot use its right to offset the effect of a challengeable subsidy under the *SCM Agreement* by means of a countervailing duty. Therefore, regarding the imposition of countervailing duties, the only rules applicable to agricultural products are those of *GATT 1994* Art. VI and *SCM Agreement* Part V. These provisions can be applied to green box subsidies, because there is no conflict between these provisions and *AoA* Art. 6 and Annex 2. The requirements for challengeability are defined in the *SCM Agreement*. In order to be countervailed, the green box measure has to cause injury.

Currently, green box subsidies can also be challenged under *SCM Agreement* Part III if they cause adverse effect, under *GATT 1994* Art. XVI if they cause serious prejudice and under Art. XXIII 1(b) if they impair or nullify a previous concession. Green box subsidies can also be challenged under *SCM Agreement* Art. 7, which establishes remedies for subsidies that cause injury, nullification or impairment, or serious prejudice. Therefore, if they cause injury, they can

⁷²⁴ See *AoA* Annex 2.

⁷²⁵ See *AoA* Art. 13 (a)(i)(ii)

⁷²⁶ See *AoA* Article 13 (a) (ii)

⁷²⁷ See *AoA* art 13 a iii

be countervailed under *SCM Agreement* Part V or challenged under the special procedures of *SCM Agreement* Art. 7. If they nullify or impair benefits, they can be challenged under *GATT 1994* Art. XXIII:1 (b).

If the complainant decides to challenge the measure under *GATT 1994* Art. XXIII 1(b) through DSU Art. 26:1, the panel has to analyze whether the challenged measure conflicts with a covered agreement and nullifies or impairs any benefit given to the complainant. If there is no breach, the complainant has to present a detailed justification regarding the challenged measure that does not conflict with any agreement, and the respondent has no obligation to withdraw the measure if nullification or impairment is found. Arbitration procedures of DSU Art. 21 can be used, and an agreement between the parties can provide for compensation.

Green box subsidies are now actionable under *SCM Agreement* Part III (Art. 5, 6 and 7). If they cause injury, they can be either countervailed under *SCM Agreement* Part V or challenged under Art. 5. The concept of injury in *SCM Agreement* Art. 5 has the same sense as in *GATT 1994* Art. VI and *SCM Agreement* Part V; therefore, whether green box subsidies are causing an impact on all relevant economic factors and indices impacting the state of the industry must be evaluated.⁷²⁸ It must be demonstrated that there is a causal relationship between the subsidized imports and the injury to the domestic industry, and the authorities should examine all the known external factors that might also injure the domestic industry.⁷²⁹

⁷²⁸ It “includes actual and potential decline in output, sales, market share, profits, productivity, return on investments, or utilization of capacity; factors affecting domestic prices; actual and potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investments and, in the case of agriculture, whether there has been an increased burden on government support programmes.” *SCM Agreement* Art. 15.4

⁷²⁹ Factors that might be relevant for such determination are “volumes and prices of non-subsidized imports of the product in question, contraction in demand or changes in the patterns of consumption, trade restrictive practices of and competition between the foreign and domestic producers, developments in technology and the export performance and productivity of the domestic industry.” *SCM Agreement* Art. 15.5

A claim challenging a green box measure under *SCM Agreement* Art. 5(b), which establishes nullification or impairment of benefits accruing directly or indirectly to other members must meet the requirements described above for challengeability under *GATT 1994* Art. XXIII, because the *SCM Agreement* states that Art. 5(b) has the same sense as that established in *GATT 1994*. The last possibility of actionability under *SCM Agreement* Art 5 is item c, which regulates subsidies that cause serious prejudice to the interests of other Members. In this case, the green box measure has to cause a) displacement of imports or displacement of the exports of a third country, b) significant price undercutting or significant prices suppression, price depression or lost sales or c) an increase in the world market share of a particular agricultural product of the subsidizing Member.⁷³⁰

Displacement has to be proved by an increase in the market share of the subsidized product, by its remaining constant in circumstances where it would have declined if there was no subsidization or if the market share of the subsidized product declines slower than it normally would if there was no subsidization. Price undercutting can be proved by a comparison between prices of the subsidized product with prices of a non-subsidized, like product supplied in the same market.⁷³¹

In order to be classified as a green box subsidy, the measure has to be minimally or non-distortive. Therefore, it would be unusual if green box measures would cause any of the effects required by the *SCM Agreement* for actionability: a) to displace, b) to cause an increase in the world market share or c) to cause price undercutting. However, if the challenged green subsidy suffers the process of box-shifting, it distorts trade, and in this case, this type of green box measure can cause adverse effects in the sense of *SCM Agreement* Art. 5.

⁷³⁰ See *SCM Agreement* 6.4.

⁷³¹ See *SCM Agreement* 6.5.

An analysis of the three types of adverse effects shows that, apparently, item b, which regulates nullification or impairment of benefits, has the lower thresholds for challengeability. As has been seen, the list of the economic factors to prove injury is long. Besides, proving displacement, price undercutting or an increase in the world market share of the subsidized product also requires an evaluation of several market-effect factors, which makes challengeability under the requirements of *SCM Agreement* items a and c more difficult.

Taking into account the information delineated herein, the conclusion is that, after the expiry of the Peace Clause, green box subsidies have become challengeable if they cause adverse effects, especially if they have suffered the process called box shifting already analyzed in this study. Even after this re-categorization, these new green box subsidies are still subject to challenges that apply to their previous designations, amber or blue, because they continue to be trade distorting and continue to not comply with Annex 2 of the *Agreement on Agriculture*.

Therefore, taking into account that there is no conflict among the AoA, *SCM Agreement* and *GATT 1994* in regulating green box measures, these Agreements are applied together to regulate challengeability, as the table below suggests:

Table 6: The Challengeability of Green Box Subsidies after the Expiry of the Peace Clause

	<i>GATT 1994</i> Art. XVI	<i>GATT 1994</i> Art. XXIII (a, via Art. II), (b) under DSU 26.1	<i>SCM</i> <i>Agreement</i> Art. 3 (via WTO DSS or special procedures <i>SCM</i> <i>Agreement</i> Art. 4)	<i>SCM</i> <i>Agreement</i> Part III (via WTO DSS or special procedures <i>SCM</i> <i>Agreement</i> Art. 7)	<i>SCM</i> <i>Agreement</i> Part V
Green Box Subsidies	Yes, if it causes serious prejudice	Yes, if it nullifies or impairs any benefit, even with no violation	Yes, under <i>SCM</i> <i>Agreement</i> 3.1(b), if given for the use of domestic over imported goods	Yes, if it causes any of the adverse effects listed in <i>SCM</i> <i>Agreement</i> Art. 5	Yes, if it causes injury in the sense of the <i>SCM</i> <i>Agreement</i> and <i>GATT</i> <i>1994</i>

Green box subsidies that cause adverse effects can be challenged under the WTO dispute settlement system by countervailing action, use of the special procedures listed in *SCM Agreement* Art. 7 or under DSU Art. 26.1 and 2 if it is chosen by the complainant for a claim under *GATT 1994* Art. XXIII:1 (b). If the complainant challenges the green box measure under *GATT 1994* Art. XVI, it must use the WTO dispute settlement system. Prior to the creation of the WTO, if the complainant challenged a green box subsidy only under *GATT 1994* XVI, the one available remedy would be a discussion with the subsidizing Member about the possibility of limiting the subsidization. Currently, a violation of *GATT 1994* Art. XVI can be brought under the DSU and be settled in the WTO dispute settlement system. This means that the parties can procrastinate on compliance through DSU Arts. 21.3(c), 21.5 and 22.6. The same will happen

with a challenge under *GATT 1994* Art. XXIII:1(a). If the complainant challenges the measure under *GATT 1994* Art. XXIII:1(b), the matter can be resolved under DSU Art. 26:1 and 2, respectively; these procedures were meant to be simpler and faster than the ordinary DSU proceedings.

If there is a violation of *SCM Agreement* Part III Arts. 5 and 6, the matter can be resolved either through the WTO dispute settlement system or through *SCM Agreement* Art. 7, which was designed to be more expeditious than the ordinary proceedings of the WTO, however Art. 7 takes precedence over DSU procedures to the extent of any difference. Countervailing duties have special procedures to resolve a dispute according to *SCM Agreement* Part. V, because they are trade remedies. A measure can be challenged at the same time under *SCM Agreement* Parts III and V, if both do not seek relief regarding the effects of the subsidies in the national market of a Member.⁷³²

Therefore, in terms of how long a measure would take to remedy a purportedly adverse effect of a green box subsidy, which is a relevant component of determining the efficiency of the challenge, the procedures set out in *SCM Agreement* Art. 7 could be simpler and faster. If it is a non-violation claim brought under *GATT 1994* Art. XXIII, the dispute settlement procedures also can be simpler, because of DSU Art. 26. The comparison is made with the WTO ordinary procedures of dispute settlement that, as was seen, can take a decade to resolve a case because of DSU Arts. 21.3(c), 21.5 and 22.6. and other possibilities for procrastination.

⁷³² *SCM Agreement* n. 35.

III.5.2 Non-Green Box Subsidies

Amber box programs are the most trade distortive domestic support measures subject to reduction commitments detailed in Part IV of Member's schedules."⁷³³ Blue box programs are direct payments under production-limiting programs and are not subject to commitments to reduce domestic support if a) such payments are based on a fixed area and yields, b) such payments are made on 85% or less of the base level of production or c) livestock payments are made on a fixed number of heads.⁷³⁴

During the Peace Clause period, amber and blue box subsidies had less protection from legal challengeability than did green box subsidies. They were vulnerable to countervailing duty actions; however, injury had to be proved under *SCM Agreement* Part V and *GATT 1994* Art. VI, and Members were obliged to exercise due restraint⁷³⁵ when taking action. Since the expiry of the Peace Clause, there is no more need to exercise due restraint in the challenges under *GATT 1994* Art. VI and *SCM Agreement* Part V. Injury is a requirement for countervailing duties; therefore, it still has to be proved for a successful challenge.

Additionally, subsidies categorized in the amber and blue boxes were not actionable under the legal provisions of *SCM Agreement* Arts. 5 and 6, *GATT 1994* Article XVI and non-violation nullification or impairment claims if they did not give support in excess of the 1992 marketing year levels.⁷³⁶ Since the expiry of the Peace Clause, the 1992 level excess requirement for challenging these subsidies under the WTO provisions has not existed.

⁷³³ See *AoA* Art. 6.1.

⁷³⁴ See *AoA* Art. 6.5(a).

⁷³⁵ "[T]he ordinary meaning of 'due restraint' is 'a proper, regular, and reasonable demonstration of self-control, caution, prudence and reserve'". *Mexico – Olive Oil* *supra* note 308 at paras. 7.44-81.

⁷³⁶ See *AoA* Art. 13(b).

Currently, amber and blue box subsidies can also be challenged under *SCM Agreement* Part III if they have an adverse effect.

It is interesting to note that, while AoA Art. 13(a)(ii) exempted green box measures from actions based on *SCM Agreement* Part III, AoA Art. 13(b)(ii) exempted non-green box measures only from *SCM Agreement* Arts. 5 and 6, which meant that non-green subsidies were purportedly actionable under *SCM Agreement* Art. 7, even during the peace years. However, even though the Peace Clause did not directly prohibit the actionability of non-green measures under the remedy procedures of *SCM Agreement* Art. 7, it prohibited them under Arts. 5 and 6, which are the substantive provisions that have to be used to justify the procedural remedy established in Art. 7.

Currently, non-green box measures can be challenged under *SCM Agreement* Art. 7, because *SCM Agreement* Arts. 5 and 6 can be used as well. Therefore, if the measures cause injury, they can be countervailed under *SCM Agreement* Part V or challenged under the special procedures of *SCM Agreement* Art. 7 and the WTO DSU..

The concept of injury in *SCM Agreement* Art. 5 has the same sense as that in *GATT 1994* Art. VI and *SCM Agreement* Part V; therefore, as with green-box measures, there must be an evaluation of whether green box subsidies are having an impact on all relevant economic factors and indices having an impact on the state of the industry. A causal relationship between the subsidized imports and the injury to the domestic industry has to be demonstrated, and the authorities must examine all known external factors that might also injure the domestic industry.

In the same way, if non-green box measures nullify or impair benefits, they can be challenged under *GATT 1994* Art. XXIII:1 (a) by virtue of *GATT 1994* Art. II and under *GATT 1994* Art. XXIII:1 (b) according to the procedures of DSU 26:1. The procedures are the same as explained for green box measures in the section above.

The last possibility for actionability under *SCM Agreement* Art 5 is item c, which regulates subsidies that cause serious prejudice to the interests of other Members. In this case, non-green box measures also have to cause a) displacement, b) significant price undercutting or its variables or c) an increase in the world market share of the subsidizing Member in a particular agricultural product.⁷³⁷ Displacement and price undercutting can be proved in the same way as for green-box measures.⁷³⁸

Prior the expiration of the Peace Clause, the accepted interpretation, according to the AoA, was that there was no risk of actionability for a Member that applied non-green box subsidies, due to the fact that the subsidies conformed fully to the requirements of AoA Arts. 6.2, 6.4 and 6.5, which meant that the reduction commitments had been met. Since the expiry of the Peace Clause, the *AoA*, *SCM Agreement* and *GATT 1994* apply together, because there is no conflict among the provisions of these Agreements for amber and blue box subsidies. This means that, even if non-green box measures comply with the limits of the *AoA*, they can be challenged under the *SCM Agreement* if they cause adverse effects according to the table below.

Table 7: The Challengeability of Non-Green Box Subsidies after the Expiry of the Peace Clause

⁷³⁷ See *SCM Agreement* 6.4.

⁷³⁸ See *SCM Agreement* 6.5.

	<i>GATT 1994</i> Art. XVI	<i>GATT 1994</i> Art. XXIII (a via Art. II), (b) under DSU 26.1	<i>SCM Agreement</i> Art. 3 (via WTO DSS or special procedures <i>SCM Agreement</i> Art. 4)	<i>SCM Agreement</i> Art. 6 and 7 (via WTO DSS or special procedures <i>SCM Agreement</i> Art. 7)	<i>SCM Agreement</i> Part V
Non Green Box Subsidies	Yes, if they causes serious prejudice	Yes, if they nullify or impair any benefit, even with no violation	Yes, under <i>SCM Agreement</i> 3.1(b) if given for the use of domestic over imported goods	Yes, if they cause any of the adverse effects listed in <i>SCM Agreement</i> Art. 5	Yes, if they cause injury in the sense of the <i>SCM Agreement</i> and <i>GATT 1994</i>

Non-green box subsidies that cause adverse effects can be challenged under the WTO dispute settlement system, through countervailing action, under the special procedures of *SCM Agreement* Art. 7 or under the DSU Arts. 26.1 and 2 if these are chosen by the complainant for a claim under *GATT 1994* Art. XXIII:1 (b). In the same way as green box measures, if the complainant challenges non-green box measures under *GATT 1994* Art. XVI, it must use the WTO dispute settlement system, and the dispute can take several years, because of DSU Arts. 21.3(c), 21.5 and 22.6. The same will happen with a challenge under *GATT 1994* Art. XXIII:1(a) that has to be brought into the WTO dispute settlement system. If the complainant challenges the measure under *GATT 1994* Art. XXIII:1(b), the matter can be resolved more quickly under DSU Art. 26:1.

If there is a violation of *SCM Agreement* Art. III, the matter can be resolved either through the WTO dispute settlement system or more quickly through *SCM Agreement* Art. 7.

Countervailing duties have special trade remedy procedures, according to *SCM Agreement* Part V.

AoA Article 6 establishes that domestic support reduction commitments, expressed in terms of Total Aggregate Measurement Support and “Annual and Final Bound Commitment Levels” of each Member shall apply to all of a Member’s domestic support measures in favor of agricultural producers, with the exception of green-box measures. As shown above, since the expiry of the Peace Clause, any WTO Member can challenge non-green box subsidies, even if there is compliance with *AoA* reduction commitments. The panel and the Appellate Body will judge whether these subsidies are causing adverse effects under the *SCM Agreement*. If the answer is yes, then there is the likelihood that they will be considered illegal.

However, it should be stated that the concept of automatic violation does not exist in the WTO system. Non-green box domestic support measures conforming to the *AoA* do not automatically cause adverse effects, including serious prejudice, to the interests of another Member within the meaning of Articles 5 and 6 of the *SCM Agreement*. In this case, the same rule applied to green box subsidies is applied to non-green box subsidies. In order to be considered challengeable under *SCM Agreement* Part III, the measures have to cause adverse effects to the interests of other Members.

III.5.3 Agricultural Export Subsidies

Under the Peace Clause, agricultural export subsidies were even more protected than amber and blue box measures. For example, they were vulnerable to countervailing duty actions only if due restraint was exercised in the action and upon a determination of injury based on

volume, effect on prices or consequent impact in accordance with *GATT 1994* Art. VI or *SCM Agreement* Part V.⁷³⁹ Hence, agricultural export subsidies were not challengeable under the legal challenges of *SCM Agreement* Articles 3, 5 and 6 and *GATT 1994* Article XVI, even if the level of the subsidies were higher than the 1992 marketing year levels. Non-violation, nullification or impairment theories were not protected by the Peace Clause, because agricultural export subsidies are highly distortive, and it is unlikely that they can be challenged under a non-violation clause. However, since the expiry of Peace Clause, they can be challenged even if the total amount is less than the levels specified in each Member's schedule.

Currently, agricultural export subsidies are prohibited under *SCM Agreement* Part II and can be challenged with no proof of adverse effect because they are completely prohibited under *SCM Agreement* Art. 3. This also means that the special procedures outlined in Art. 4 can be used for a simpler and faster dispute resolution. Because there is no conflict between the *AoA* and the *SCM Agreement* to regulate this type of subsidy, even if it complies with the *AoA* schedules, it can be challengeable under the *SCM Agreement*.

Subsidies can also be challenged under the *SCM Agreement* Part III if they cause adverse effects and under *GATT 1994* Art. XVI if they cause serious prejudice. If they cause injury, they can also be countervailed under *SCM Agreement* Part V. It is relevant to note that a causal relationship between the subsidized imports and the injury to the domestic industry also has to be demonstrated, and authorities should examine all the known external factors that might also injure the domestic industry.⁷⁴⁰

A claim challenging agricultural export subsidies under *SCM Agreement* Art. 5(c), as with a claim challenging other types of subsidies, has to prove a) displacement, b) price

⁷³⁹ See *AoA* Art. 13(c)(i).

⁷⁴⁰ *SCM Agreement* Art. 15.4 and 15.5.

undercutting or c) an increase in the world market share of the subsidizing Member in a particular agricultural product.⁷⁴¹ However, the simpler way to challenge agricultural export subsidies is under *SCM Agreement* Art. 3, because no adverse effect has to be proved, since subsidies are completely prohibited. Any type of adverse effect, either injury, impairment of benefit or serious prejudice is presumed in this case.

AoA Art. 8 rules that “[e]ach Member undertakes not to provide export subsidies otherwise than in conformity with this Agreement and with the commitments as specified in that Member’s Schedule.” *AoA* Art. 9 defines export subsidies as being subject to reduction commitments under the *AoA*. It is clear that the export subsidies defined in *AoA* Art. 9.1 can only be given within the limits determined by the Agreement and according to the quantity previously committed. No subsidy can be given to any agricultural product if that subsidy is not specified in the Agreement,⁷⁴² with the exception of developing countries, who can give the export subsidies listed in subparagraphs (d) and (e) of Article 9.1, provided that these are not applied in a manner that would circumvent reduction commitments.⁷⁴³

AoA Art. 10.1 permits export subsidies that are not listed in Article 9.1, both for scheduled and unscheduled products, only if such subsidies are not “applied in a manner which results in, or which threatens to lead to, circumvention of export subsidy commitments.” In addition, non-commercial transactions will not be used to “circumvent such commitments.” *SCM Agreement* Art. 3.1 “except as provided in the *Agreement on Agriculture*” prohibits subsidies contingent upon export performance⁷⁴⁴ and upon the use of domestic over imported goods.⁷⁴⁵ Reading the *AoA* and the *SCM Agreement* together, someone could incorrectly interpret

⁷⁴¹ See *SCM Agreement* 6.4.

⁷⁴² See *AoA* Article 3.3

⁷⁴³ See *AoA* Article 9.4

⁷⁴⁴ See *SCM Agreement* Article 3.1(a).

⁷⁴⁵ See *SCM Agreement* Article 3.1(b).

(ignoring there is no conflict between the Agreements to regulate agricultural export subsidies) that if export subsidies comply with the *AoA* limits they cannot be challengeable under the *SCM Agreement*, even after the expiry of the Peace Clause.

In *US – Subsidies on Cotton* the US argued that that “Step 2 payments to domestic users of upland cotton were included and complied with the United States’ domestic support reduction commitments pursuant to Article 6.3 of the *Agreement on Agriculture*.” It asserted that because these payments were permitted under the Agriculture Agreement, they could not be in violation of the *SCM Agreement*. The Panel rejected the US defense, finding no conflict between the domestic support provisions of the *AoA* and *SCM Agreement* Art. 3.

As shown by the application of the practical and theoretical methods and according to the WTO panels and the AB, there is no conflict among the *AoA*, *SCM Agreement* and *GATT 1994* to regulate agricultural subsidies, which means that they are applied together to regulate this type of subsidy, as the table below shows:

Table 8: The Challengeability of Agricultural Export Subsidies after the Expiry of the Peace Clause

	<i>GATT 1994</i> Art. XVI	<i>SCM Agreement</i> Art. 3 (via WTO DSS or	<i>SCM Agreement</i> Art. 6 and 7 (via WTO DSS or	<i>SCM Agreement</i> Part V
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		special procedures <i>SCM Agreement</i> Art. 4)	special procedures <i>SCM Agreement</i> Art. 7)	
Agricultural Export Subsidies	Yes, if it causes serious prejudice	Yes, even if they comply with the <i>AoA</i> limits	Yes, if it causes any of the adverse effects of <i>SCM Agreement</i> Art. 5	Yes, if it cause injury in the sense of <i>SCM Agreement</i> and <i>GATT 1994</i>

Agricultural export measures are the most trade-distortive type of subsidy. For this reason, they can be challenged under *SCM Agreement* Part II, either in the WTO dispute settlement system or by using the special procedures outlined in Art. 4, which can expedite the settlement of a dispute brought under *SCM Agreement* Art. 3. This would be the less complex way to challenge this type of subsidy. Agricultural export subsidies that cause adverse effects can be challenged under the WTO dispute settlement system, through countervailing action or under the special procedures outlined in *SCM Agreement* Art. 7 if the claim is brought under *SCM Agreement* Arts.5 and 6. If the complainant challenges agricultural export subsidies under *GATT 1994* Art. XVI, it must use the WTO dispute settlement system. The dispute can take a long time to be settled under the DSU.

According to the *SCM Agreement*, agricultural export subsidies can be challenged at the same time under *SCM Agreement* Parts III and V.⁷⁴⁶ The *AoA* regulation of agricultural subsidies is compatible with the prohibitions determined in the *SCM Agreement*. A Member can grant agricultural export subsidies consistent with *AoA* commitments without violating the *SCM Agreement* prohibition if such subsidies do not harm another WTO Member through the

⁷⁴⁶ *SCM Agreement* n. 35.

displacement of exports. That is the rationale behind the common regulation of agricultural subsidies by the *AoA*, *SCM Agreement* and *GATT 1994*.

Upon the expiry of the Peace Clause, agricultural export subsidies have not only been challengeable under *SCM Agreement* Art. 3.1, but also under Arts. 5 and 6. This means that, currently, any Member being harmed by agricultural export subsidies can countervail them or challenge the subsidizing Member under the WTO dispute settlement system or by using the special procedures outlined in *SCM Agreement* Arts. 4 and 7.

CHAPTER IV

CONCLUSION

It has been shown that the expiry of the Peace Clause altered the overlapping limits on the challengeability of agricultural subsidies, which occurred as a result of the changes in the relationship among the provisions that regulate agricultural subsidies in the *AoA*, the *SCM*

Agreement and the *GATT 1994*. According to traditional doctrine, there are two possible ways to interpret this relationship among the WTO agreements.

It has been shown, after a deeper analysis of the relationship, that the first interpretation, which stated that the AoA should apply alone to regulate agricultural subsidies because there was a conflict with the *SCM Agreement*, does not prevail. It has also been determined that the second interpretation, which reached the correct conclusion that the AoA, the *SCM Agreement* and the *GATT 1994* should be interpreted together, had a mistaken premise, because it was based on the principle of “effective interpretation” and not on the view that there was no conflict among these Agreements. If there were, the most specific had to apply, and the consequence would be that agricultural subsidies could not be challenged under the *SCM Agreement*.

The Peace Clause’s expiry brought in a new arrangement for the challengeability of agricultural subsidies, and not only in respect of non-violation cases and countervailing duties. It made the challengeability of green, domestic/actionable and export subsidies possible under the *SCM Agreement*. Upon the expiry of the Peace Clause, there was a certain degree of uncertainty about whether the *SCM Agreement* and the AoA could be cumulatively applied to domestic agricultural subsidies and what the new limits of challengeability were, especially between the AoA and the *SCM Agreement*.

Before the expiry of the Peace Clause, there were some extravagant estimations of a possible flood of agricultural subsidy challenges under the WTO dispute settlement system. It was feared that most of the subsidizing Members would be held accountable for their agricultural subsidies in the WTO disputes. None of these possibilities occurred because it continues to be significantly complex to prove adverse effects under the *SCM Agreement*.

Although the expiry of the Peace Clause did make all agricultural subsidies challengeable under the *SCM Agreement*, it did not change the *SCM Agreement* requirements for challengeability. This means that the result of a WTO agricultural subsidy complaint cannot be determined *a priori*. Each case has its own idiosyncrasies, and the fulfillment of requirements for challengeability can only be identified on a case-by-case basis. To use an example, currently, all agricultural subsidies are actionable under *SCM Agreement* Part III, but this does not necessarily mean that such subsidies are automatically forbidden. They still have to cause adverse effects, which includes serious prejudice, in order to be challenged under the WTO dispute settlement system. According to WTO rules, an agricultural subsidy has to be withdrawn upon the DSB’s condemnation, based upon an allegation of adverse effects.

This study proved that the chances of success in exposing agricultural subsidies to WTO challenges will also depend on the category of the agricultural subsidy in question. The expiry of the Peace Clause did not change the fact that agricultural export subsidies are more trade distortive than green box subsidies. The level of proof will depend on the specifics of each case, but this study has suggested that the expiry of the Peace Clause has brought about “new” limits for the challengeability for agricultural subsidies, according to the proposed table below.

Table 9: The Challengeability of Agricultural Subsidies upon the Expiry of the Peace Clause

	<i>GATT 1994</i> Art. XVI	<i>GATT 1994</i> Art. XXIII (a, via Art. II), (b) under DSU 26.1	<i>SCM Agreement</i> Art. 3 (via WTO DSS or special procedures	<i>SCM Agreement</i> Part III (via WTO DSS or special	<i>SCM Agreement</i> Part V
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			SCM Agreement Art. 4)	procedures SCM Agreement Art. 7)	
Green Box Subsidies	Yes, if they cause serious prejudice	Yes, if they nullify or impair any benefit, even with no violation	Yes, under 3.1(b)	Yes, if they cause any of the adverse effects outlined in SCM Agreement Art. 5	Yes, if they cause injury in the sense of the <i>SCM Agreement</i> and <i>GATT 1994</i>
Non Green Box Subsidies	Yes, if they cause serious prejudice	Yes, if they nullify or impair any benefit, even with no violation	Yes, under 3.1(b)	Yes, if they cause any of the adverse effects outlined in SCM Agreement Art. 5	Yes, if they cause injury in the sense of the <i>SCM Agreement</i> and <i>GATT 1994</i>
Agricultural Export Subsidies	Yes, if they causeserious prejudice	Yes, but unlikely	Yes, even if they comply with the AoA limits	Yes, if they cause any of the adverse effects outlined in SCM Agreement Art. 5	Yes, if they cause injury in the sense of the <i>SCM Agreement</i> and <i>GATT 1994</i>

Source: *AoA* Art. 21.1; *WTO Agreement* Art. II.2; *Argentina – Footwear (EC) supra* note 609 , *Indonesia – Autos supra* note 227 para 14.28; *Guatemala –Cement I supra* note 640 at para. 65; *US – Gasoline supra* note 10 at 23; Max Plank, *Encyclopedia of Public International law* ed. By Rudolf Bernhardt (New York: North Holland Pub. Co, 1990 at 468; Wilfred Jenks, “The Conflict of Law-Making Treaties” (1953) 30 *The British Yearbook of International Law (BYIL)* 425.; Dominique Carreau & Patrick Juillard, *Droit International Ecomique* (Paris : Dalloz, 2003) at para. 369.

The standards for challengeability became more complex after the Uruguay Round. This study showed that the *GATT 1947* system used to consistently limit agricultural subsidies, which did not occur after the implementation of the WTO. The Peace Clause was one of the important factors that contributed to the difficulties in challenging agricultural subsidies during the WTO years. The failure of the AoA in diminishing agricultural trade barriers to integrate agriculture in

the WTO system and the lack of a full modalities agreement because of the inconclusive Doha Round are also factors to be considered. The result is that the goals of substantial and progressive reductions in agriculture support established in the preamble and in *AoA* Art. 20 have not been achieved so far.

It is generally accepted that the creation of the WTO was an advance towards trade liberalization. This study has demonstrated that agricultural subsidization in the WTO still has to overcome major obstacles to be on the same path to liberalization as non-agricultural products. The Peace Clause was one of the main reasons for this. It could be argued, on the other hand, that the WTO brought in the *SCM Agreement*, with new provisions to challenge subsidies, which could purportedly increase the possibilities for challengeability. However, challengeability under the *SCM Agreement* was limited during the peace years as well. Besides, the *SCM Agreement* has several market-effect requirements, first mentioned in the TRSC, to challenge agricultural subsidies, which did not exist in the *GATT 1947*. These requirements made the challengeability of agricultural subsidies significantly more difficult.

In order to challenge agricultural subsidies under the *GATT 1947*, it was not necessary to prove a link between cause and effect. In the *SCM Agreement*, one or several of the following requirements are required for challengeability: a) a displacement⁷⁴⁷ which was established as a requirement for proof of serious prejudice,⁷⁴⁸ b) price undercutting, price suppression or price depression⁷⁴⁹ and c) an increase in the world market share in a particular subsidized agricultural product. They are all market-effect requirements. It could be said that the *GATT 1947* only had one market-effect requirement for the challengeability of agricultural export subsidies, which was the concept of “more than an equitable share of the world export trade” under Art. XVI. This

⁷⁴⁷ See *SCM Agreement* Art. 6.3(a) and (b)

⁷⁴⁸ See *SCM Agreement* Art. 6.1

⁷⁴⁹ See *SCM Agreement* Art. 6.3(c)

sole market-effect condition was largely criticized as being an inaccurate *GATT 1947* provision, but even so, Art. XVI was substantive rule that limited agricultural subsidies during the *GATT 1947* years.

As has been seen, the concept of material injury⁷⁵⁰ in the *GATT 1947* was “any damage to an established industry or a retard to the establishment of a domestic industry.”⁷⁵¹ Under the WTO’s regime, the concept of injury had to be proved through an examination of the impact of the subsidized imports on the domestic industry, which had to include an assessment of several micro- and macro-economic factors and indices on a non-exhaustive list.⁷⁵² The result is that under the WTO, most of the requirements to challenge agricultural subsidies have to be proved through econometric analysis. This makes challengeability more difficult and, in some cases, might lead to an analysis of the law almost exclusively focused on economics.

The *GATT 1947* system was perhaps more simple and primitive, and the complexity brought about by the WTO was the price paid for a more elaborate system. First, a more elaborate system does not mean a fairer or better system. Second, the WTO brought in relevant advances in several aspects of the international trading system’s regulations, but agriculture was different. The WTO did not succeed in limiting or impeding agricultural subsidization’s practices. The WTO’s data demonstrate that, in 1995 (the year the Uruguay Round agreements

⁷⁵⁰ Material injury is a requirement for countervailability of GATT Art. VI and Part V of the *SCM Agreement* that regulate trade remedies: countervailing duties, anti-dumping and safeguard measures. The regulation of trade remedies under the WTO is a different obligation. The WTO rules only give legal guidance for the national application of these remedies on the country of the imported goods. However, the exporting country still can challenge any of these trade remedies under the WTO dispute settlement system alleging that the importer Member violated its obligations.

⁷⁵¹ See GATT Art. VI 6(a).

⁷⁵² See *SCM Agreement* Art. 15.4

went into effect), most of the heaviest subsidizing Members were subsidizing in lower levels than they were authorized to by the limits established by the WTO agreements.⁷⁵³

The conclusion is that, after the creation of the WTO, the agricultural sector became even more distorted by subsidies and tariff policies. Agriculture was the only sector in the WTO that had three-digit tariffs and safeguard measures to apply significant duties with no proof of injury besides other distortive measures.⁷⁵⁴ Even though the GATT had a primitive and simple system, there was a legal rationale for condemning agricultural subsidies. On the other hand, the more sophisticated WTO legal framework, as was seen, made challenging agricultural subsidies more difficult.

The case analysis of both periods corroborates this hypothesis. It goes against the opinion of some scholars, because they normally evaluate the efficiency of the GATT and the WTO through an analysis of compliance and a comparative analysis of procedural rules, which includes rules on dispute settlement. After qualitative⁷⁵⁵ analyses of both the rules and cases, the conclusion is that the lack of complexity in the GATT dispute settlement system did not hinder condemnation of agricultural subsidies in a clear and consistent way during the GATT years, a situation that did not occur after the creation of the WTO, with its more elaborate dispute settlement system.

Therefore, as a result of the analysis provided throughout this thesis, it can be concluded that, after the expiry of the Peace Clause, agricultural export and domestic support subsidies have become more vulnerable to legal challenges than during the Peace period. However, this does not

⁷⁵³ The US was using only 26.9% of its permitted AMS, the EC 63.6%, Japan 73.1%, Mexico 4.8% and Canada 15%. Tim Josling, "The Uruguay Round Agreement on Agriculture: A forward-Looking Assessment" *Paper prepared for a seminar at the Organisation for Economic Cooperation and Development (OECD), 1998*. (Paris: Institute for International Studies, 1998) at Table 7.1.

⁷⁵⁴ Melaku Geboye Desta, *The Law of International Trade in Agricultural Products: From GATT to the WTO Agreement on Agriculture*. (London: Kluwer Law International, 2002) at 427.

⁷⁵⁵ Analysis of the (subject matter) material rules and the legal rationale of the cases about agricultural subsidization in contrast with procedural rules.

mean that there is a free ride for challenges to agricultural subsidies. A successful challenge against green, non-green and export subsidies has to overcome not only higher *SCM Agreement* standards but also some non-orthodox strategies of defense under the *AoA*, such as box and product shifting. These strategies can still be used, because agriculture still is a highly distorted sector in the WTO system.

Challenging agricultural subsidies remains a challenge after the expiry of the Peace Clause. This study has demonstrated that it was possible during the GATT years, highly improbable during the peace period and significantly complex upon the expiry. The end of the Peace Clause, in some ways, can assist Members trying to remedy some adverse effects of agricultural subsidization through the WTO dispute settlement system; but it does not resolve the problem. Among other measures, a full agreement on modalities and the completion of the Doha Round are necessary for the accomplishment of the goals established in the *AoA* of substantial and progressive reductions in agricultural support and protection. In this way, the scenario Desta described below can be changed:

[A]griculture still stands alone as the sector where export subsidies are expressly and generously – albeit selectively – permitted under WTO law; where three-digit tariffs are common and four-digit rates may not be impossible to find; where significant additional duties can be introduced in the name of “safeguard measures” regardless of injury considerations and in the most unpredictable of ways; where a proven trade-distortive and injurious domestic support program may escape challenge under the nullification or impairment provisions of the multilateral trading system.⁷⁵⁶

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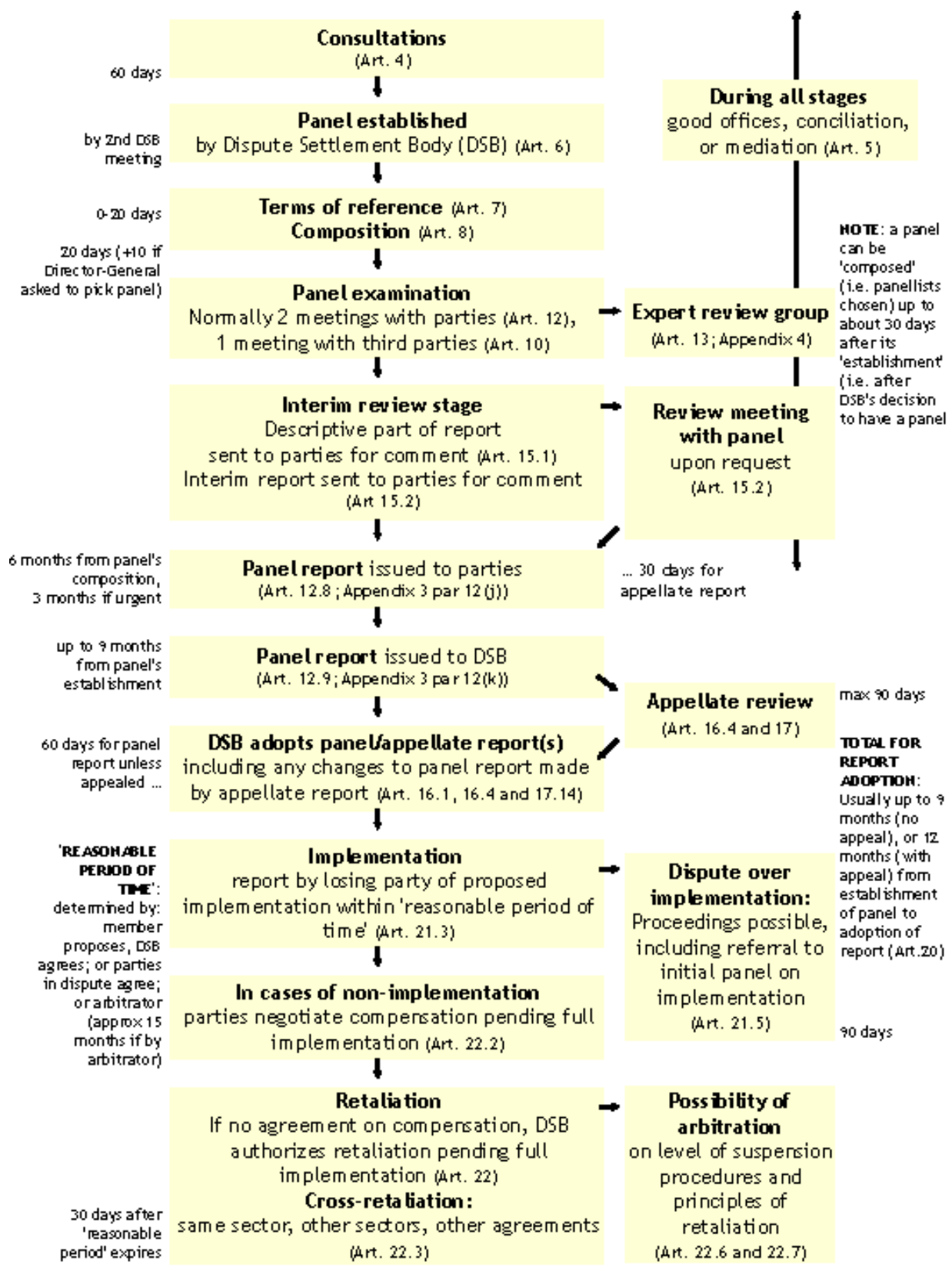
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ANNEX I
The WTO Panel Process



ANNEX II

Countervailing Duties under the *SCM Agreement*

The requirements to initiate an investigation were the same established in TRSC Art.2.1: (a) subsidy, (b) injury according to the meaning of *GATT 1994* Art. VI and (c) a causal link between the subsidized imports and the alleged injury. It means the substantive requirements to countervail subsidies did not change and were first established in *GATT 1994*, however procedural rules were considerable inflated by the *SCM Agreement*. Art. 11 established what were the formal elements and information that an application shall have in order to be accepted by an investigation authority.

It has to have the identity of the applicant and a description of the volume and value of the domestic production of the like product. If the application is made on behalf of domestic industry, it shall contain a list of all known domestic producers of the like product and an approximate volume and value of its production. The application also has to have a complete description of the subsidized products, the exporting countries and the exporters and also a list of importers in the national market. Evidence of the existence, amount and nature of the subsidy in question and evidence of the alleged injury to the domestic industry are also needed. The evidence of injury to domestic industry has to have an evolution tied to the volume of the subsidized imports, the effect of such imports on prices of the like products on domestic market and on domestic industry.⁷⁵⁷

The application has to be supported by at least 50 per cent of the total production of the like product produced by a portion of the domestic industry that either supported or opposed the application. The investigation cannot proceed however if the application of domestic producers

⁷⁵⁷ See *SCM Agreement* Art. 11.2 (i), (ii), (iii) and (iv).

that expressed support does not represent more than 25 percent of total production of the like product produced domestically. The investigating authorities can initiate an investigation with no application if there is sufficient evidence of subsidy, injury and causal link to justify the investigation. The evidence of both subsidy and injury has to be simultaneously analyzed, with the decision to initiate an investigation starting no later than provisional measures may be applied.⁷⁵⁸

The investigation shall be terminated if the volume of subsidies is *de minimis* (less than 1 per cent ad valorem) or subsidy or injury is negligible. In cases where products are not imported directly from the countries of origin but from an intermediate country, the provisions of the *SCM Agreement* for countervailing measures should be applied to the country of origin and the importer. Investigations cannot hinder customs clearance and they cannot take longer than 18 months after their initiation.⁷⁵⁹ The period for the investigation in the TRSC was 12 months and these formal requirements to submit the application to ask for countervailing duties were not required in the Tokyo Round Subsidies Code. The *SCM Agreement* considerably increased procedural rules for countervailing duties, especially to determine the concept of evidence.

SCM Agreement Art. 12 established a procedural system to evaluate the evidence of subsidization to make possible an affirmative or negative decision about countervailing duties. Exporters, foreign producers or any interested Member⁷⁶⁰ that receive a questionnaire have 30 days to reply. Oral information can be given by interested parties but it must be submitted in writing in order to be used by investigating authorities. Confidential information can be

⁷⁵⁸ See *SCM Agreement* Art. 11.4, 11.5 and 11.6.

⁷⁵⁹ *Ibid.* at 11.8-11.11.

⁷⁶⁰ Interested Members are the exporter, the importer of a product that is being investigated or a trade or business association that gather a majority of producers, exporters or importers of these products, a producer of a like product in the importing Member or a trade or business association in the same way in the territory of the importer or any other interested Member. *SCM Agreement* Art. 12.9(i)-(ii).

protected, but in this case a non-confidential summary must be submitted. Investigating authorities may carry on investigation in the territory of other Members and in the premises of a firm if it does not object to. If access is refused, preliminary and final determinations will be based on the facts available.⁷⁶¹

After the initiation of the investigations, consultations take place so that interested Members can have an opportunity to reach a mutually agreed solution. The *SCM Agreement* provisions of Art. 12 that regulated consultations have almost the same writing to the TRSC Art. 3 provisions. Both articles of the TRSC and *SCM Agreement* titled consultations have four paragraphs, each one with similar writing and same objective.

The first paragraph of TRSC Art. 3 and *SCM Agreement* Art. 12 set forth the possibility of consultations after the establishment of the investigation. The second paragraph did not determine a specific period of consultations but determined that it had to provide the possibility of clarifying the factual situation to work towards an agreed solution. The third paragraph clarified that consultations should take a reasonable period of time but could not hinder investigating authorities in reaching preliminary or final determination, whether affirmative or negative. The fourth paragraph of both Agreements established that the Member who conducts the investigation must allow, if asked, access to non-confidential evidence for the Member whose export is being investigated.

SCM Agreement Art. 14 establishes some guidelines for investigating authorities to calculate subsidies given by exporting Members. Its application has to be transparent and adequate. The article excludes from the concept of subsidies that can be countervailed: government provision of equity capital; a loan by a government, a loan guaranteed by a government and the provision or purchase of goods or services by a government. However, in

⁷⁶¹ *Ibid.* at 12.1-12.12.

some specific cases, they can be considered to be subsidies. For example, if the loans, services or goods are provided with different values than the Member would receive on the market, the difference would be considered a subsidy. The TRSC does not give general guidelines for investigating authorities to calculate subsidies that can be countervailed and does not provide any specific definition of domestic industry. Besides, the definition of injury in the TRSC is not as detailed as in the *SCM Agreement*.

As seen, the definition of injury in the TRSC included several market effect factors and the *SCM Agreement* copied the paragraphs that defined subsidies from the TRSC. *SCM Agreement* Art. 15.1 defined the meaning of the word “injury” of *GATT 1994* Art. 6 through market-effect parameters in the same exact words defined in the TRSC. It was necessary to have an objective examination of a) the volume of the subsidized imports and their impact on prices in the domestic market of like products (a significant increase of the volume of subsidized imports); and b) the impacts of such imports on domestic producers (price undercutting, prices depressing or prevention of prices’ increase on the importing country).⁷⁶² It is relevant to observe that the concept of injury for countervailing duties is the same for *SCM Agreement* Part V.

Also, in the *SCM Agreement* it is relevant to note that Art. 15.2 established that none of these factors can give a precise guidance to the determination of injury.⁷⁶³ In the same way that it is stated in the TRSC, there is an assumption in the *SCM Agreement* that, even though requirements to determine injury are being created, there is no clear and complete concept of injury. Therefore, regarding substantive provisions, the *SCM Agreement* did not evolve much from the TRSC, not even in the concept of injury.

⁷⁶² See *SCM Agreement* Art. 15.1 and TRSC Art 6.1 and 6.2.

⁷⁶³ *Ibid.* at 15.2.

SCM Agreement Art. 15.4 replicated the provision of TRSC paragraph 3 that established the impact on the domestic industry shall take into account an evaluation of “all” relevant economic factors that interfere in the state of the importing country’s industry that might be harmed by subsidies of the exporting country.⁷⁶⁴ The *SCM Agreement* followed the complex set of economic factors described in the TRSC to determine injury. However, the same art. 15.4 states that none of these economic factors would give decisive guidance for a determination of injury. Therefore, the *SCM Agreement* kept exactly the same inaccurate concept of injury inherited from the TRSC.

The *SCM Agreement* determines that causal relationship between injury and subsidization must be determined by all relevant evidence. Investigating authorities must also examine other factors other than subsidized imports that are injuring the domestic industry. For this reason, it is important to know the volume and prices of the non-subsidized imports, contractions in demand, changes in consumption, trade restrictive practices, developments in technology and export performance and productivity of domestic industry.⁷⁶⁵ This list helps the investigating authorities determine factors that can interfere in the causal link between subsidy and injury. However, it is highly complex to determine how much a factor, such as development in technology, influences the price of an exported product being investigated.

The factors for a determination of threat of material injury are different because they are trade effects likely to arise in the future, but they are equally difficult to be determined. *SCM Agreement* Art. 15.7 provides a list of them. The investigating authorities have to look at: a) how

⁷⁶⁴ *SCM Agreement* Art. 15.4 established some economic factors that can influence in an injury determination. It is stated that the list is not exhaustive and no one of these several factors can give decisive guidance.

[A]ctual and potential decline in output, sales, market share, profits, productivity, return on investments, or utilization of capacity; factors affecting domestic prices; actual and potential negative effects on cash flow, inventories, employment, wages, growth, ability to raise capital or investment and, in the case of agriculture, whether there has been an increased burden on Government support programmes.

⁷⁶⁵ See *SCM Agreement* Art. 15.5.

subsidized imports might increase in the domestic market, b) imminent substantial increase in the capacity of the exporter, c) prices of the imports that will have a significant depressing or suppressing effect on domestic prices and d) inventories of the investigated products.

There is one paragraph in the article that says one isolated factor cannot give decisive guidance, but the total of the factors considered must lead to a conclusion that protective action is necessary in order to avoid future material injury. This paragraph states that determining injury is complex, a threat of it is even more difficult, however if these factors are combined they can give an indication of threat of injury.

SCM Agreement Art. 16 defines domestic industry as domestic producers that produces the majority or 100 per cent of a like product inside a territory. In exceptional circumstances, this territory may be divided in two for the production in question when production and demand are concentrated in different locations. In that case, countervailing duties can be applied only in the consumption's location.⁷⁶⁶

SCM Agreement Art. 17 established provisional countervailing duties that can be applied if investigating authorities gave public notice and Members and interested parties have had opportunity to submit information and make comments. Other conditions include a preliminary affirmative determination of subsidy and injury by investigating authorities, and a decision that such provisional measures are necessary to prevent injury. These provisional measures can be established through provisional countervailing duties guaranteed by cash deposits or bonds proportional to the amount of the provisionally calculated amount of subsidization. They cannot be applied sooner than 60 days from the date of the initiation of the investigation and are limited to a period not exceeding four months.

⁷⁶⁶ See *SCM Agreement* Art. 16.1 to 16.3.

TRSC Art. 5 regulated provisional measures and were the base of some of the provisions established in the *SCM Agreement*. TRSC Art. 5.2 determined the need of provisional countervailing duties be financially guaranteed according to the proportionate amount of subsidies provisionally calculated and Art. 5.4 established that provisional measures should not last more than four months.⁷⁶⁷

SCM Agreement Art. 18 inherited similar provisions about undertakings from TRSC Art .4. *SCM Agreement* established that the imposition of countervailing duties can be suspended if the government of the exporting country agrees to limit or eliminate subsidies, the exporter agrees to revise its price, and the national authority of the importing country is satisfied. However, the importing Member cannot accept the undertakings for several reasons and the evaluation of the injury can continue. *SCM Agreement* Art. 18.5 determines that price undertaking can be suggested by the importing authorities, but the exporter is not obliged to accept the suggested price.

If the exporter accepts the undertakings suggested by the importer, either on a possible limitation of exporters or on a suggested price, according to *SCM Agreement* Art. 18.6, the export might be periodically required to provide information relevant to the fulfillment of such undertakings. If the exporter fails to comply with the terms of the undertakings, application of provisional measures or definitive duties using the best information available can be applied.⁷⁶⁸ In such cases, definitive duties may apply to products entered for consumption not more than 90 days before the application of such provisional measures. Retroactive assessment does not apply in this case according to the provisions of the *SCM Agreement*.

⁷⁶⁷ *Ibid.* at Art. 5.4.

⁷⁶⁸ This is also the text of TRSC Art. 4 that was the predecessor of *SCM Agreement* Art. 18.6.

After reasonable efforts have been made to complete consultations, the investigating authority of a Member can make a final determination to impose countervailing duties. The amount countervailed has to be appropriated and must be levied in a non-discriminatory basis. It cannot be levied in excess of the level of subsidy given.⁷⁶⁹

Countervailing duties can be levied retroactively when a final finding of injury or, in some cases⁷⁷⁰ threat of injury, is determined for the period for which provisional measures, if any, have been applied. If a final finding is negative, any deposit made during the period of application of provisional measures shall be refunded in an expeditious manner. If the definitive measure is higher than the amount guaranteed by cash, deposit or bond, the difference is not collected. If the definitive duty is less than the amount guaranteed, the excess should be reimbursed. The *SCM Agreement* authorized application of countervailing duties in specific cases retroactively 90 days from the date of application of provisional measure. These provisions were established in *SCM Agreement* Art. 20 inherited from TRSC Art. 5.

There is no specific time frame for how long a countervailing duty should last but, in any case, it can be longer than 5 years. It can be reviewed provided a reasonable period of time has elapsed since the imposition of the definitive countervailing duty, which means there is no determined period of time when a review has to occur. The duration of the review, when it happens, cannot take longer than 12 months.⁷⁷¹ Each Member with national provisions on countervailing duty will maintain judicial, administrative or arbitral tribunal for a judicial review established in *SCM Agreement* Art. 21 to review administrative actions relating to final or review

⁷⁶⁹ See *SCM Agreement* Art. 19.1-4.

⁷⁷⁰ *SCM Agreement* Art. 20.2 establishes that countervailing duties can be applied retroactively “in the case of a final determination of a threat of injury, where the effect of the subsidized imports would, in the absence of the provisional measures, have led to a determination of injury.”

⁷⁷¹ See *SCM Agreement* Art. 21.1-5.

of determinations. Such tribunals will be independent of the authorities responsible for determination or review of countervailing duties.

It could be seen during the analysis of the regulation of countervailing measures by the *SCM Agreement* that most of substantive provisions, deadlines, timeframes and even procedural rules were based on TRSC regulation. The *SCM Agreement* however, considerably incremented the procedural rules of the TRSC that was supposed to determine and “clarify” substantive concepts of *GATT 1994*. However neither the TRSC nor the *SCM Agreement* gave “decisive guidance” about these substantive concepts, such as injury.

Several *SCM Agreement* provisions were born in the TRSC and therefore inherited its imperfections, inaccuracies and complex thresholds for actionability of subsidies. *SCM Agreement* Art. 5 and 6 that defined the framework of subsidies’ actionability after the Uruguay Round were originated from TRSC Art. 8. *SCM Agreement* Art. 5 has almost the same writing than TRSC Art. 8 paragraph 3 and *SCM Agreement* Art. 6 is an evolution of TRSC Art. 8 paragraph 4.

ANNEX III

Overview About the Negotiations of Agricultural Subsidies

a) The continuation of the Reform Process on Agriculture

The *AoA* Art. 20 regulates a long-term and progressive reduction of supports and determines reform is a continuous process. The Members agreed that negotiations would proceed one year before the period of implementation (2000) and would take into account: the experience of implementing reduction commitments; the effect of such reduction commitments on world trade in agriculture; non-trade concerns, special treatment for developing countries and the principles established on the preamble to establish a fair agricultural market, besides any other commitment needed to achieve these objectives.⁷⁷²

The *AoA* acknowledged that agriculture had a “built-in agenda”⁷⁷³ that started in the Uruguay Round and did not stop with the regulation of the *AoA*. Actually the Agreement recognized that its reductions commitments were not enough and more regulation was needed for trade liberalization. Therefore, according to the established in the *AoA*, Members agreed to continue the reforms to reduce commitments on agriculture. Negotiations initiated in 2000.

In November 2001, in the launch of the Doha Round in the 4th Ministerial Conference in Qatar, a continuous agenda for agricultural negotiations was defined. The Ministerial

⁷⁷² See *AoA* Art. 20.

⁷⁷³ Merlinda Ingco & Alan Winters, “Agricultural Trade Liberalization in a New Trade Round: Perspectives of Developing Countries and Transition Economies”. *World Bank Discussion Paper n° 418, 2001* (Washington D.C.: WB – ITD 2001) at 1.

Declaration⁷⁷⁴ incorporated the negotiations in agriculture that were initiated in early 2000 according to the mandate of AoA Art. 20 and incorporated another subjects to the agenda according to proposals submitted by 121 Members.⁷⁷⁵

The Declaration also confirmed the commitment to establish a fair market oriented trading system and reductions of a view to improve market access, phase out all forms of export subsidies⁷⁷⁶ and substantially reduce trading distorting domestic support. It was established that an Agreement on Modalities should be finished no later than 31 March 2003, which did not occur.

In February 2003, Stuart Harbinson, the Chair of the WTO Committee on Agriculture made public his draft on modalities. A revised draft was circulated with minor changes on March of the same year in a meeting in the Committee of Agriculture. In export competition, the draft's goal was that export subsidy commitments should be reduced to zero. For this purpose, it was determined a period of time – fast and a slow track – for the complete elimination of export

⁷⁷⁴ WTO, *Doha Ministerial Declaration*, WTO Doc. WT/MIN(01)/DEC/1 (20 Nov. 2001), online: WTO <http://http://www.wto.org/english/thewto_e/minist_e/min01_e/mindecl_e.htm#agriculture> [*Doha Ministerial Declaration*].

⁷⁷⁵ Jank and Jales gave figures about the phases of agricultural negotiations in the Doha agenda:

From March 2000 to March 2001, 45 negotiating proposals and 3 technical documents were submitted to the WTO on behalf of a total of 126 Members (89% of the organization's Membership at the time). From March 2001 onwards, revised and more detailed proposals were submitted by several countries and groups of countries... The positions held by the various parties would change significantly throughout the Doha Round. Marcos Sawaya Jank & Mario de Queiros Monteiro Jales, "On Product, Box and Blame-Shifting: Negotiating Frameworks for Agriculture in the WTO Doha Round". *Second IDB-CEPII Conference: "Economic Implications of the Doha Development Agenda for Latin American and the Caribbean"* (Sao Paulo: ICONE, 2004) at 6 [Jank & Jales, *Blame Shifting*].

⁷⁷⁶ *Doha Ministerial Declaration* included a statement for a complete phasing out of all form of export subsidies:

13. We recognize the work already undertaken in the negotiations initiated in early 2000 under Article 20 of the *Agreement on Agriculture*, including the large number of negotiating proposals submitted on behalf of a total of 121 Members. We recall the long-term objective referred to in the Agreement to establish a fair and market-oriented trading system through a programme of fundamental reform encompassing strengthened rules and specific commitments on support and protection in order to correct and prevent restrictions and distortions in world agricultural markets. We reconfirm our commitment to this programme. Building on the work carried out to date and without prejudging the outcome of the negotiations we commit ourselves to comprehensive negotiations aimed at: substantial improvements in market access; reductions of, with a view to phasing out, all forms of export subsidies; and substantial reductions in trade-distorting domestic support. *Supra* note 445 at para. 13.

subsidies: five years (ten years for developing countries) in the fast track and nine years (twelve years for developing countries) in the slow track. Sensitive products were put in the slow track list. Regarding market access, the draft proposed tariffs would have a minimum cut⁷⁷⁷ as an alternative proposal to the so-called Swiss Formula.⁷⁷⁸

In domestic support, the proposal was to maintain the category of green box subsidies but possibly amend them. All provisions of Art. 6.2⁷⁷⁹ would not only be maintained but enhanced. Blue box measures should be capped at the average level notified for the implementation years [1999-2001] and bound at the levels of Member's schedules in order to be reduced by 50 percent. The reduction should be over the period of time of five years and should be included in the Member's calculation of the AMS. The proposal for amber box subsidies was a cut by 60 percent over the period of time of five years and AoA Art. 6.3 should be amended so that AMS levels for individual products would not exceed the respective levels of the support provided in the years of 1999-2001.

A consensus was not reached and the deadline of 31 March 2003 to establish an Agreement on Modalities was missed. The impasse was transferred to Cancun Ministerial Conference where Members tried to reach at least a "framework" of the modalities Agreements, which was eventually agreed only on July 2004. Several frameworks' proposals with main figures of modalities were discussed in pre-Conference meetings, so that a conclusion could be reached in September 2003 during the 5th Ministerial Conference of Cancun.

⁷⁷⁷ WTO, *First Draft of Modalities for the Further Commitments*, WTO Doc. TN/AoA/W/1 (17 February 2003), online: WTO <http://www.wto.org/english/tratop_e/agric_e/negoti_mod1stdraft_e.htm> at 7.

⁷⁷⁸ First proposed by Switzerland in the Tokyo Round (1973-1979) negotiations on industrial tariffs, the Swiss Formula attempts to harmonize tariffs through an individual cut to each tariff line. The individual cut depends on a chosen coefficient. While high tariff rates are drastically reduced by the formula, low tariff rates suffer more limited cuts. Switzerland does not support this approach to tariff reduction in the current multilateral negotiations on agriculture. Jank & Jales, *Blame Shifting supra* note 334 at 9.

⁷⁷⁹ Subsidies to encourage agricultural and rural development and subsidies to encourage diversification from growing illicit narcotic crops in developing countries.

The Conference fostered consensus among Members to start negotiating again a possible framework for modalities. Members changed their initial irreducible position to a more flexible attitude aiming at closing an Agreement. The first initiative in this direction was a draft produced by the EU and US at a small ministerial conference in Montreal that contained a proposal of a general framework on modalities.

The proposal had main points that EU and US defined as the very core of the modalities. It was a framework of a proposal; it was not a complete document with all formulas and coefficients that normally an Agreement on modalities has to have. The draft circulated on 1 August 2003 and was designed to be a simpler document, so that it could be negotiated and agreed during the few days of the Cancun Round from 11-13 September 2003. For this reason it deliberately omitted some subjects such as treatment for developing countries and the consequence was some gaps and omissions.⁷⁸⁰

The EC-US joint proposal motivated other group of countries to present their own proposal with the same framework contained in the European and American draft. A new coalition called G-20⁷⁸¹ formed by some developing countries presented its draft,⁷⁸² as well as the Central American countries, Japan, and European and Asian group that included Switzerland and Rep. of Korea; Norway and Kenya.⁷⁸³

⁷⁸⁰ WTO, *The Compromise Draft of the EU and USA in Modalities*, WTO Doc. Job(03)/157 (1 August 2003), online: WTO <<http://docsonline.wto.org/gen.search/asp>>

⁷⁸¹ The 20 countries that formed and named the coalition and signed the joint proposal for a framework on modalities were Argentina, Bolivia, Brazil, Chile, China, Colombia, Costa Rica, Cuba, Ecuador, El Salvador, Guatemala, India, Mexico, Pakistan, Paraguay, Peru, Philippines, South Africa, Thailand and Venezuela.

⁷⁸² WTO, *Agriculture – Framework Proposal of the Ministerial Conference, Fifth Section, Cancun, 10-14 September 2003*, WTO Doc. WT/MIN(03)/W/6 [previously circulated as Job(03)/162/Rev.1] (4 September 2003), online: WTO <<http://docsonline.wto.org/gen.search/asp>> [*G-20 Draft on Modalities*].

⁷⁸³ WTO, *The Cancun Framework Proposals*, online: WTO <http://www.wto.org/english/tratop_e/agric_e/negs_bkgrnd21_props3_e.htm>

The G-20 Draft on Modalities called for substantial reduction on domestic support practices, even though it did not proposed any number, formula or coefficient of reduction because it followed the framework-format suggested by the EC-US joint proposal. The proposal for domestic subsidies was to reduce all trading distorting support measures on a product specific basis and determine a percentage of difference between lower and upper limits of support. Products that benefited from subsidies above the average should be subject to upper levels of reduction with a minimum cut of all trade distorting domestic subsidies. It also proposed the elimination of all blue box subsidies, reduce “de minimis” limits and AMS support and a cap or reduction for green box subsidies.⁷⁸⁴

With regard to export subsidies the draft suggested the elimination of all forms of export subsidies over a period of time as well as any officially supported export credits, guarantee and insurance programmes. It was different from the EC-US joint proposal that suggested the elimination not for all products. There was also a provision in the G-20 Draft for Modalities for additional disciplines to prevent commercial displacement. With regard to market access, it was proposed a blended formula to reduce tariffs through a percentage of reduction of tariff lines and a minimum average cut to avoid tariff escalation.⁷⁸⁵

Pre-Cancun coalitions of Members were being formed with the goal to negotiate agricultural subsidization and market access with the US and EU.⁷⁸⁶ Some of these coalitions

⁷⁸⁴ *G-20 Draft on Modalities supra* note 781 at 1.

⁷⁸⁵ *Ibid.* at 3.

⁷⁸⁶ Jank nominates the coalitions:

[C]oalitions also emerged in the aftermath of the EC-US paper, such as the “Friends of Multifunctionality” (G-10) [Bulgaria, Iceland, Israel, Japan, Liechtenstein, Mauritius, Norway, South Korea, Switzerland and Taiwan], which strongly supported new exceptions based on the concept of non-trade concerns (NTC); the “Alliance for Strategic Products and a Special Safeguard Mechanism” (G-33), which demanded specific measures to protect vulnerable sectors in developing countries; and the Group of Ninety (G-90), which drew together Least Developed Countries (LDCs) and Members of the African Union (AU) and the Africa-Caribbean-Pacific (ACP) Group. Jank & Jales, *Blame Shifting supra* note 334 at 7.

such a group formed by Members of Central America circulated their draft on modalities. It was similar to the G-20 but focused on special and different treatment for developing countries.⁷⁸⁷

The chairperson of the General Council, Carlos Perez del Castillo, included a draft of a framework on agriculture as Annex A of his and Director-General's draft of Cancun Ministerial Declaration on 31 August 2003. It was an attempt of Castillo and Supachai Panitchpakdi, the WTO Director-General, to help Members to reach an Agreement on agricultural modalities.⁷⁸⁸

The draft called for substantial reductions in any type of trade-distorting measures. In domestic support the proposal was to reduce the AMS levels and "de minimis" by a percentage, reduce and establish an annual linear reduction for blue box measures. No significant proposal to change amber and green box was made and it called for a phasing out of only a part agricultural export subsidies, as the joint draft of EC-US had proposed. The draft suggested a reduction of tariffs through a blended formula different for developed and developing countries, but with more modest cuts if compared with the G-20's draft.

Castillo's Text was discussed by Members during Cancun Round and more papers were circulated about the Castillo's proposal, which made possible a new annex in the new draft of the declaration of the Round. This annex was coordinated by Luis Ernesto Derbez, the Mexican Foreign Minister that was the chairperson of the Cancun Conference. This document dubbed

⁷⁸⁷ The draft suggested an average tariff cut and a minimum tariff cut on tariffs of developed countries with a cap for tariff lines that exceeded a maximum percentage. There were several provisions about differential and special treatment for developing countries, but no suggestion of reduction on export and domestic subsidies. WTO, *Joint Text by Dominican Republic, Honduras, Nicaragua and Panama of the Ministerial Conference, Fifth Section, Cancun, 10-14 September 2003*, WTO Doc. WT/MIN(03)/W/10 [previously circulated as Job(03)/164] (5 September 2003), online: WTO <<http://docsonline.wto.org/gen.search/asp>>

⁷⁸⁸ WTO, *Annexes to the Draft Cancun Ministerial Text*, WTO Doc. Job(03)/150/Rev.1 (24 August 2003), online: WTO <<http://docsonline.wto.org/gen.search/asp>> [*Castillo's Text*]

Derbez Text⁷⁸⁹ was circulated on 13 September 2003, one day prior to the conclusion of the Conference and, for this reason, could not be discussed by Members in detail; therefore, no Agreement was reached.

The Derbez Text was different from the previous draft (Castillo's Text) especially because it suggested an extension of the Peace Clause. However, this draft kept some similarities with the previous one, especially in export competition because both texts did not call for a phasing out of export subsidies for all products. As in the Castillo's Text, in terms of domestic support, this draft proposed reductions of AMS levels and "de minimis" and proposed to establish an annual linear reduction for blue box measures. The Derbez Text also proposed a review for green box measures not suggested in the previous draft. In market access it also suggested a blended formula to establish a variable to reduce tariff rates for processed goods and a cap for tariff peaks.⁷⁹⁰

The Cancun Ministerial Meeting ended in deadlock and no Agreement was reached over the Derbez Text. Therefore, negotiations on agriculture stopped from September 2003 to August 2004 with no sessions in the WTO Agriculture Committee and the deadline to complete the Doha Round on 1 January 2005 was jeopardized.

However, on 1 August 2004 an Agreement was reached containing a framework for modalities on agriculture, the so called *July 2004 Package* that broke Cancun's deadlock.⁷⁹¹ The

⁷⁸⁹ WTO, *Preparations for the Fifth Session of the Ministerial Conference, Draft Cancun Ministerial Text, Second Revision*, WTO Doc. Job(03)/150/Rev.2 (13 September 2003), online: WTO <<http://docsonline.wto.org/gensearch/asp>> [Derbez Text].

⁷⁹⁰ *Ibid.* at A1 – A4.

⁷⁹¹ WTO explains the surroundings of the so called July 2004 Package:

Ten months later the Cancun deadlock was broken. Shortly after midnight on 1 August 2004, the WTO's 147 Member governments approved a package of Agreements that includes an outline (or "framework") to be used to complete the "modalities" on agriculture. The deal was struck after delegations negotiated intensively day and night for two weeks, culminating in a gruelling, non-stop session involving key ministers and ambassadors, that began at 5pm on Friday 30 July and lasted almost 24 hours. During the

negotiations started in Geneva on March 2004. The new chairperson, Ambassador Tim Groser of New Zealand developed a different strategy to conduct the negotiations. He suggested the delegations to first hear all the proposals and then discuss it to resolve the points of disagreement. His role was to focus on the process and not on the content of the proposals, as had happened before with other previous chairpersons.

In the transparency meetings, delegations reported their proposals for agriculture. The chair received 52 formal negotiating proposals, 32 Secretariat background papers and 99 unofficial papers, as well as several framework drafts. After these meetings, delegations and some coalitions as the Cairns Group, the G-10, G-20 and G-33⁷⁹² started to meet on private basis.⁷⁹³

Delegations finally agreed to try to define an Agreement with a framework of agricultural modalities with no figures by the end of July. Meetings took place in Geneva on April and June and paved the way for the *July 2004 Package*. On June 30 Ambassador Groser took a more active role in the negotiations and circulated his report, the chairperson's assessment. This document contained the structure of the framework on modalities that was later agreed on July.

In this document, Groser stated that he could realize convergence among all delegations in some specific issues, such as an overall cut in trade distorting support measures; amber box subsidies should have greater cuts because they are more distortive; specific products that had to

fortnight, there were several meetings of heads of delegations, intensive consultations and countless gatherings of various groups, with a number of trade ministers participating. WTO, *WTO Agricultural Negotiations, The Issues and Where We Are Now*, online: WTO <http://www.wto.org/english/tratop_e/agric_e/negs_bkgrnd00_contents_e.htm#download> [The July 2004 Package].

⁷⁹² See Annex IV with the countries and coalitions of the negotiations. *Ibid.* at 83-86.

⁷⁹³ The July 2004 Package *supra* note 761 at 14.

have specific caps and reductions levels of AMS and reductions for “de minimis” levels for developed countries.⁷⁹⁴

The blue box subsidies were a major point of disagreement because, as seen in previous drafts, some Members wanted to increase this box and others wanted to put all blue box subsidies into the amber box. Groser did not support any proposal but stated that blue box were potentially distortive and for this reason should be limited, but there had to be flexibility in some exceptional circumstances to implement these limits. In his opinion, there was consensus about the need of more surveillance and monitoring for green box subsidies to guarantee they would not distort trade.⁷⁹⁵

On export subsidies, it was clear that an Agreement on framework should contemplate a fixed date for the phasing out of all export subsidies. On market access the chairman pointed out the main criticisms about the Swiss and the blended formula and tried a new methodology to calculate tariff cuts that was called the “tiered approach”. It was an attempt to circumvent the barriers that some Members had with the Swiss and the blended formula. This approach established stiffer cuts for higher bands.⁷⁹⁶

In the last week of July 30 ministers went to Geneva for the General Council meeting to try to close an agreement on the framework of modalities. Negotiations were intense and a first draft of the Agreement was circulated on 16 July with the agriculture framework in annex A. A second draft was circulated on July 30 and on August 1 Members closed an agreement over a third draft after 24 hours of negotiations.

⁷⁹⁴ WTO, *Minutes of Meeting, Held in the Centre William Rappard on 30 June 2004, Trade Negotiations Committee*, WTO Doc. TN/C/M/13 [restricted] (12 August 2004), online: WTO <http://www.wto.org/english/tratop_e/agric_e/negs_bkgrnd23_julypack_e.htm> at 10 [*Chairperson’s Assessment*].

⁷⁹⁵ *Ibid* at 11.

⁷⁹⁶ *Ibid* at 12-15.

The *July 2004 Package* – even though it was concluded in August 1 – contains a framework for modalities in Annex A that had been negotiated for four years.⁷⁹⁷ The Agreement confirmed that the deadline of 1 January 2005 to conclude the Doha Round would not be met and also, for the first time, there was a recognition that cotton was of vital importance for developing countries, especially the Least Developed Countries [LDC]s.⁷⁹⁸ Annex A with the Framework for Establishing Modalities in Agriculture had seven sessions: domestic support, export competition, market access, least-developed countries, recently acceded Members, monitoring and surveillance and ended with other issues’ section.

The preamble of the Annex stated that, under the mandate of paragraph 13 of the Doha Ministerial Declaration, the goal was to build on the long term of the *Agreement on Agriculture*⁷⁹⁹ and a fair and market-oriented trading system. The Agreement was a framework document, which means, as stated before, that there were no definitive figures on modalities, but key aspects without details, which meant negotiation was still needed for a “full” Agreement on modalities.

The document called for reform in the three pillars of agriculture to be approached in a “balanced and equitable manner”⁸⁰⁰ and emphasized development and non-trade concerns. It also established a paragraph on surveillance to ensure full transparency and clarify some issues of interest that had not been agreed, such as sectoral initiatives and differential on export taxes.

⁷⁹⁷ Agricultural negotiations after the Doha Round started on 2000, one year prior the end of the implementation period established in the Uruguay Round.

⁷⁹⁸ WTO, *Doha Work Programme, Decision adopted by the General Council on 1st August 2004*, WTO Doc. WT/L/579 (2 August 2004), online: WTO <http://www.wto.org/english/tratop_e/agric_e/negs_bkgrnd23_julypack_e.htm> at 2 .

⁷⁹⁹ This was the same objective stated on AoA Art. 20 that was the base for the Doha Ministerial Declaration.

⁸⁰⁰ *Supra* note 381 at A1.

On domestic support, the *July 2004 Package* assured differential treatment for developing countries and established that developed countries should make deeper cuts on higher support levels. There was a compromise of each Member to make substantial reduction in the overall level of its trade-distorting support and in “de minimis” levels, according to a tiered formula. As stated, under this formula, Members that have higher level of support measures are subject to higher level of overall reductions. Therefore, AMS levels would have to be substantially reduced under the same tiered approach.⁸⁰¹

Blue box subsidies shall not exceed 5 percent of a Member’s average total value of agricultural production during a period of time to be established in the negotiations. Green box support will have to be reviewed and clarified to have no or minimal trade-distorting effect on production, which means they will have to be monitored. All forms of export subsidies will have to be phased out by a credible end date.⁸⁰²

One relevant consequence of *July 2004 Package* was that it made possible the consolidation of alliances of countries that changed the traditional epicenter of negotiations – the US, EU, Canada and Japan. Currently, there are other developed and developing countries that also gathered representation in the negotiations that took the leadership in the Cancun Ministerial Meeting. This shift was consolidated with the Agreement of the *July 2004 Package* and challenged in Hong-Kong Ministerial Conference.

On October 2004 Members started to work to have a full Agreement of modalities on agriculture. From October 2004 to July 2005, in almost every month, the delegations got together

⁸⁰¹ *Ibid* at para. 6.

⁸⁰² *Ibid* at A2.

to negotiate the modalities Agreement in informal and formal special sessions.⁸⁰³ It was called the “technical phase” preparatory to the Hong-Kong Ministerial Conference.

The Sixth Ministerial Conference took place in Hong-Kong from 13 to 18 December 2005. For agricultural negotiations the goal was to reach a full Agreement on modalities with formulas and other details to determine levels of reduction for agricultural subsidies and for several tariffs.⁸⁰⁴ An Agreement with this level of ambition was not possible, but some advance occurred. Annex A of the Ministerial Declaration set up what had been agreed on agriculture.

First, the declaration reaffirmed the goal to finish Doha successfully in 2006 and emphasized the relevance of the development aspects of the Doha work programme. Under these goals reaffirmed in the *July 2004 Package*, three bands for reductions in final bound total AMS in the overall cut in trade-distorting domestic support with higher linear cuts in higher bands. Higher cuts for higher levels of support had already been determined in *July 2004 Package*, but Hong-Kong negotiations established bands for reductions.⁸⁰⁵

⁸⁰³ The WTO explains the environment of the negotiations in 2004 right after the July Package:

By November [2004], a pattern had emerged. The formal meetings (the formal “Special Sections” of the Agriculture Committee), usually at the end of the week, were mainly for taking decisions and for Members to put some of their comments on the record. Informal meetings (informal “Special Sections”) were for general comments and assessments, and for first readings of each technical issue. Consultations at a more technical level (“open-ended” consultations, meaning all Members could attend, in a smaller room) allowed delegates to go into some highly specialized questions in greater detail. Some delegates said they benefited from hearing the discussion among their more specialist colleagues. WTO, *The July 2004 Package and August Decision. After the Framework: Modalities*, online: WTO <http://www.wto.org/english/tratop_e/agric_e/negs_bkgnd23_julypack_e.htm>

⁸⁰⁴ WTO Ministerial Conferences take place at least once every two years to provide political guide for the organization from its highest decision-making body. WTO, *The Sixty WTO Ministerial Conference*, online: WTO <http://www.wto.org/english/thewto_e/minist_e/min05_e/min05_e.htm>

⁸⁰⁵ The Declaration established the numeric limits and the Members that would be in the three bands:

There is a working hypothesis of three bands for overall cuts by developed countries. There is a strongly convergent working hypothesis that the thresholds for the three bands be US\$ billion 0-10; 10-60; >60. On this basis, the European Communities would be in the top band, the United States and Japan in the second band, and all other developed countries at least in the third band. For developing countries, there is a view that either developing countries are assigned to the relevant integrated band (the bottom) or that there is a separate band for them. WTO, *Doha Work Ministerial Declaration Adopted on 18 December 2005, Ministerial Conference, Sixth Session, Hong-Kong 13-18 December 2005*, WTO doc. WT/MIN(05)/DEC (22 December 2005), online: WTO <<http://docsonline.wto.org/gen.search/asp>> at A2.

It was also established that blue box payments would have to be reduced but less than the overall reduction for amber box subsidies, but Members could not agree on the level of this cut. Negotiations about green box subsidies did not evolve much. It was established that it had to be ensured through an efficient mechanism of surveillance that they cause no or minimal trade-distorting effects, especially for developing countries.⁸⁰⁶

On export measures Members agreed for the first time in a Ministerial Declaration that all forms of export subsidies and all export disciplines had to be completely eliminated by the end of 2013. However, this deadline should be confirmed on 30 April 2006 when a full Agreement of modalities should be reached and complete the negotiations of the disciplines on export credits, export credit guarantees or insurance programmes, exporting state trading enterprises and food aid as part of a full modalities Agreement.⁸⁰⁷ Developing countries would continue to benefit from the exception of giving export subsidies to reduce costs of marketing exports of agricultural products and internal transport and freight charges on export shipments of agricultural products.⁸⁰⁸

On market access the proposal was to create four bands for structuring tariff cuts, but the relevant thresholds still have to be negotiated. Sensitive products also had to have a different treatment but no formula was defined as a part of the full modalities *Agreement on Agriculture*. Special and different treatment was reaffirmed as a relevant aspect to be considered in the formulas and it was agreed that much still have to be done in market access negotiations. For this reason the declaration stated that Members had to intensify work to fulfill the Doha objectives to

⁸⁰⁶ *Ibid.* at para 5.

⁸⁰⁷ *Ibid.* at A4.

⁸⁰⁸ The Ministerial Declaration established that developing countries could keep the benefits from the provision of AoA Art. 9.4 for five years after the end date for elimination of all forms of export subsidies.

establish a full Agreement on modalities no later than 30 April 2006 and to submit comprehensive draft of schedules based on modalities no later than 31 July 2006.

On 2006 Members met in Geneva from 28 June to 1 July to try to reach a full Agreement on modalities. Negotiations were suspended on the end of July after six representatives of main countries in the negotiations fail to reach an Agreement. A draft with suggestions and the divergent proposals of the Members was circulated on 12 July 2006. In the Draft, Ambassador Crawford Falconer, the chairman of the Committee on Agriculture, stated that "unless or until there is such emergent consensus [on a modalities full Agreement], one has to respect the substantive positions of Members." Therefore, his draft was not an "elegant document" in his own words because it had gathered several different proposals with no consensus.⁸⁰⁹

In 2008 Members negotiated another package of modalities rules that was considered a significant advance for agricultural regulation and a step toward the conclusion of the Doha Round. However, differently from the 2004 package, the 2008 package was not a completely agreed document. There was deadlock in some issues but the negotiations evolved and some gaps could be narrowed. Numbers started to be defined to reduce domestic subsidies, a date to phase out export subsidies was confirmed and specific percentages of reductions for bands of products were negotiated in market access.

Meetings took place in Geneva from 21 to 30 July but negotiations started on September 2007, which led to around 240 hours of negotiations. There was deadlock in some issues but the negotiations evolved and some gaps could be narrowed, especially because numbers became to be defined for reduction of domestic subsidies; a date to phase out export subsidies was

⁸⁰⁹ WTO, *Draft Possible Modalities on Agriculture, Committee on Agriculture, Special Section*, WTO Doc. TN/AoA/W/3 (12 July 2006), online: WTO <http://www.wto.org/english/tratop_e/dda_e/modalities06_e.htm> at 2 [*Draft on Modalities 2006*].

confirmed; and, specific percentages of reductions for bands of products were negotiated in market access.

So far, there is no Agreement of a complete modalities Agreement, but negotiations considerably evolved from July 2008 on. On domestic support, green box measures will be considerably modified according to the last draft circulated on December 2008.⁸¹⁰ Members altered paragraph 6 of *AoA Annex II* that has a list of green box subsidies with the goal to make sure they are really decoupled from production levels. There were also modifications to guarantee food aid to developing countries and severe monitoring and surveillance to impede that distort trading subsidies could be classified under the green box.⁸¹¹

Amber box subsidies have to be cut to 70 percent by EU, 60 percent by US and Japan and 45 percent by the rest of the Members. Some other developed countries will have bigger cuts, such as Switzerland, Norway and others. They also will be capped at an average level of support that was notified by the Members in 1995-2000.⁸¹² Blue box subsidies will have to be limited to 2,5 percent of the average total value of agricultural production in the 1995-2000 base period by developed countries and to 5 percent by developing countries with a cap per product.⁸¹³

It was corroborated that export subsidies will have to be eliminated by the end of 2013 and half of this by the end of 2010. Provisions on export credit, guarantees and insurance, international food aid and exporting state trading enterprises are still being revised.⁸¹⁴ On market access, higher tariffs will have deeper cuts. For developed countries the cut would vary from 50

⁸¹⁰ WTO, *Revised Draft Modalities for Agriculture, Committee on Agricultural, Special Section*, WTO Doc. TN/AoA/W/4/Rev.4 (6 December 2008), online: WTO <http://www.wto.org/english/tratop_e/agric_e/chair_texts08_e.htm> at 2 [*Draft on Modalities 2008*].

⁸¹¹ *Ibid.* at 39-43.

⁸¹² *Ibid.* at 4-6.

⁸¹³ *Ibid.* at 10-12.

⁸¹⁴ *Ibid.* at 30-31.

percent for tariffs below 20 percent to 70 percent for tariffs above 75 percent subject to a 54 percent minimum average with some limitations for tariffs above 100 percent. Developing countries will have to cut by two thirds of the equivalent tier for developed countries with a maximum average of 36 percent. Some products will have smaller cuts according to flexibilities for sensitive and special products.

It can be realized that a full modalities Agreement is closer, the framework was agreed in 2004 through the July Package and figures are converging for a complete Agreement. However, the WTO single undertaking rule states that nothing is agreed until everything is agreed, so the completion of a full modalities *Agreement on Agriculture* has significantly evolved as the Draft of December proved, but negotiations still have to take place to seal a complete Agreement.

b) An Assessment of the Ongoing Negotiations on Agriculture under the Doha Round

The negotiations to reduce trading distortive measures on agriculture continue under the mandate of paragraph 13 of the Doha Declaration that was originally given by *AoA* Art. 20. This Article regulates a long-term and progressive reduction of supports and determines reform is a continuous process. The negotiations after the Uruguay Round started in 1999 because Members agreed that negotiations would proceed one year before the period of implementation (2000).

As verified in the previous section, *AoA* Art. 20 set up the parameters for the continued process of agricultural negotiations that shall take into account: the experience of implementing reduction commitments; the effect of such reduction commitments on world trade in agriculture; non-trade concerns, special treatment for developing countries and the principles established on

the preamble to establish a fair agricultural market; besides any other commitment needed to achieve these objectives.⁸¹⁵

Paragraph 13 of the Doha Declaration quoted *AoA* Art. 20 to recall the long-term objective in agricultural negotiations, the need to establish a fair and market-oriented trading system to reduce distortions on agriculture. It specifically quoted the need to improve policies on market access, phase out all forms of export subsidies and substantially reduce trade-distorting domestic support. As seen, it was agreed by Members that export subsidies have (at least was negotiated in this manner) to be eliminated by the end of 2013. Tariff cuts and domestic support reductions are being negotiated, even though there is no a complete Agreement about figures of these cuts and reductions.

Special and differential treatment for developing countries was emphasized in paragraph 13 of the Doha Declaration. It stated that special treatment should be reflected in the schedules of concessions and commitments of the Members and in the rules and disciplines negotiated in agriculture. The goal to take into account developing countries' needs in an effective manner, which means establish to them less stringent rules for cuts on import tariffs and on reduction of subsidies. Different figures on tariff cuts and reduction on subsidies are being negotiated for developing countries so far.

Essentially, the Doha mandate confirmed the *AoA* goals to imposed specific commitments and schedules to reduce support and protectionist measures in the three pillars of agriculture: domestic support, market access and export competition. The goal was to liberalize trade in each of these areas and, also, to strengthen the agricultural system with clearer and more defined rules and disciplines. The verification whether these goals will be reached will only be

⁸¹⁵ See *AoA* Art. 20.

possible after a full Agreement on modalities is completed and after the confirmation whether all export subsidies were completely phased out on 2013.

It can be stated that market access' negotiations have been negotiated with the goal to impose more stringent rules on agricultural trade distorting practices, specially for Non-Tariff Barriers [NTB]s to diminish distortions in highly protected markets. The tariffication helped in this process, however it was not enough to prevent distortions –especially because bound tariffs after tariffication are much higher than the real applied tariffs, among other distortions that remained such us illegal import licensing. Besides, tariffication only affected around 14 percent of OECD agricultural trade.⁸¹⁶

Therefore, the current negotiations under the mandate of *AoA* Art.20 and paragraph 13 of the Doha Declaration still have several distortive practices to correct and get agricultural negotiations on the same path of liberalization as other sectors such as industrial goods.

Other distorting practices that still remain are tariff-rate quotas (TRQ) that were created to provide a minimum level of import opportunities for products previously protected by non-tariff barriers. As explained before, this process created two levels of import tariffs: one relatively low on imports up to a specified level; the other on imports above this level, subject to a higher tariff when over quota. Now that all implementation periods of the Uruguay Round have finished, there is no more space in the current agricultural regulation for distortive practices that were negotiated as a price to pay for the Agreement.

It can be stated that one advance of the *AoA* in domestic support provisions was the explicit recognition of the direct relation between domestic agricultural policies and international

⁸¹⁶ See Merlinda Ingco, ed., *Agriculture, Trade and WTO: Creating a Trade Environment for Development*. (Washington: The World Bank, 2002).

trade distortions. However, it is not enough anymore, now it is time for these distortions to be identified and completely eliminated. Actually, *GATT 1994* had already recognized that domestic subsidies could distort trade in Art. XVI,⁸¹⁷ but there was no specific regulation for domestic support measures in the *GATT 1994*.

The reason is that regulating agriculture was always a delicate issue for international law because of the sensitivity of national policies. Nevertheless, the international community currently not only recognizes how trading distortive domestic subsidies can be, but also urges for reforms in the Doha Round to minimize these effects. As seen, one of the main aspects of the domestic measures' legal framework was the classification of subsidies on boxes that set apart domestic policies that were deemed (a) not to, or only to a minimum extent, distort trade (green box measures) and (b) all other policies that distort trade (amber box measures, blue box measures and some other exempt measures). It is time for considerable reduction of amber and blue box measures and effective methods of surveillance that avoid box shifting from distortive boxes to the green. Negotiations are going to this direction but they must be concluded to effectively apply these reductions.

In the Uruguay Round some WTO Members had to, purportedly; reduce agricultural domestic support levels, such as administered prices, input subsidies and producer payments that were not accompanied by limitations on production. As explained before, domestic support reductions in agriculture were implemented through a commitment to reduce the total aggregate measurement of support (AMS) for each country. However, these measures were not enough to

⁸¹⁷ GATT Art. XVI establishes that:

[I]f any contracting party grants or maintains any subsidy [which include domestic support], ... it shall notify the CONTRACTING PARTIES ... In any case in which it is determined that serious prejudice to the interests of any other contracting party is caused ... the contracting party granting the subsidy shall ... discuss with the other contracting party ... the possibility of limiting the subsidization.

effectively reduce distortive support and, for this reason, negotiations in this matter are still going on under the Doha mandate.

Export subsidies negotiations were planned to be reduced in the Uruguay Round. However, high levels of distortions were maintained especially by the US and EU. WTO Members were committed to reduce the volume of subsidized exports by 21 percent and the expenditure on subsidized export by 36 percent. These reductions were suppose to take place from the 1986-90 base period level over a six-year implementation period (10-year period for developing countries), on a product-specific basis. Export subsidies on products not subsidized in the base period were supposed to be banned. As export subsidies kept distorting and interfering in trade, they were called to be completely phased out in 2013. If it is going to happen is a question that only time can answer.

The last implementation period for *AoA* reductions was completed in 2004 and Doha Round is still being negotiated, even though it was supposed to be completed by 1 January 2005. It can be stated that much of the success of the liberalization process of the Uruguay Round depends on a successful development of the Doha Round. As seen, the three pillars (market access, export subsidies and domestic support) of agriculture established during the Uruguay Round have several flaws, but they can be addressed and potentially corrected in Doha, as the negotiations are pointing to.

The Doha round negotiations continue and there are lot of skepticism about the agricultural negotiations. However, from a legal perspective, the *AoA* made possible the replacement of several distortive measures by numeric commitments, even though it is not clear whether it meant a step forward toward trade liberalization. These numeric commitments were

established and quantitative restrictions were agreed upon for all three pillars, providing the basis and the legal framework for the current negotiations in the Doha Round.

The experience to date from the *AoA* implementation period shows that agricultural policy reform effects have been, to say the least, modest. There are some good directions pointed by the *July 2004 Package* and the current negotiations, however, nothing is agreed until everything is agreed⁸¹⁸ and the Doha Round has to be concluded for a right assessment whether agricultural negotiations are finally being addressed in a way to effectively reduce supports and tariffs.

Now that tariffication has already being implemented and the *July 2004 Package* established the framework for a full Agreement on modalities, negotiations on agriculture have a solid base to be completed. The new players have an important role to play in the reform process of agriculture and in the conclusion of the negotiations,⁸¹⁹ but the same question that remain for the Doha Round since the Uruguay Round's negotiations: is it possible to reach the right equation between agricultural subsidies' reductions from old major WTO players and market access opportunities from the new WTO alliances of Members? If yes, the Doha Round can be unlocked with the consequent advances on agricultural trade liberalization.

⁸¹⁸ The statement composes the WTO principle of single undertaking.

⁸¹⁹ See Annex III

ANNEX IV
Group of Countries and Alliances in the WTO Agricultural Negotiations

Groups

Phase 1: countries, alliances and proposals

Members that submitted proposals and technical papers in Phase 1, with an indication of groupings and alignments based on joint-authorship

Details at: http://www.wto.org/english/tratop_e/agric_e/negoti_e.htm

1. Albania (transition: domestic support)
2. Angola (African Group)
3. Antigua and Barbuda (Caricom)
4. Argentina (Cairns Group + MERCOSUR)
5. Australia (Cairns Group)
6. Barbados (Caricom + small island developing states + non-trade concerns)
7. Belize (Caricom)
8. Benin (African Group)
9. Bolivia (Cairns Group + "MERCOSUR+" 1, 2)
10. Botswana (African Group)
11. Brazil (Cairns Group + MERCOSUR)
12. Brunei (ASEAN)
13. Bulgaria (transition: domestic support, market access)
14. Burkina Faso (own proposal + African Group)
15. Burundi (own proposal + African Group + non-trade concerns)
16. Cameroon (African Group)
17. Canada (Cairns Group + own proposal on market access, supplementary proposal on domestic support)
18. Central African Republic (African Group)
19. Chad (African Group)
20. Chile (Cairns Group + "MERCOSUR+" 1, 2)
21. Colombia (Cairns Group + "MERCOSUR+" 2)
22. Congo (African Group)
23. Congo, Democratic Rep (own proposal + African Group)
24. Costa Rica (Cairns Group + "MERCOSUR+" 1)
25. Côte d'Ivoire (African Group)
26. Croatia (transition: domestic support, market access)
27. Cuba (developing country grouping 1, 2, 3 + small island developing states)
28. Cyprus (non-trade concerns)
29. Czech Republic (transition: domestic support, market access + non-trade concerns)
30. Djibouti (African Group)
31. Dominica (small island developing states + Caricom)
32. Dominican Republic (developing country grouping 1, 2, 3)
33. Egypt (own proposal + African Group)
34. El Salvador (developing country grouping 1, 2, 3)
35. Estonia (transition: market access + non-trade concerns)
- 36–51: EU (Austria, Belgium, Denmark, Finland, France, Germany, Greece, Ireland, Italy,

- Luxembourg, Netherlands, Portugal, Spain, Sweden, UK) (own proposals + non-trade concerns)
52. Fiji (non-trade concerns)
 53. Gabon (African Group)
 54. The Gambia (African Group)
 55. Georgia (transition: domestic support, market access)
 56. Ghana (African Group)
 57. Grenada (Caricom)
 58. Guatemala (Cairns Group)
 59. Guinea (African Group)
 60. Guinea Bissau (African Group)
 61. Guyana (Caricom)
 62. Haiti (developing country grouping 1, 2, 3)
 63. Honduras (developing country grouping 1, 2, 3)
 64. Hungary (transition: domestic support, market access)
 65. Iceland (non-trade concerns)
 66. India (own proposal + developing country grouping 3)
 67. Indonesia (Cairns Group + ASEAN)
 68. Israel (non-trade concerns)
 69. Jamaica (small island developing states + Caricom)
 70. Japan (own proposal + non-trade concerns)
 71. Jordan
 72. Kenya (own proposal + developing country grouping 1, 2, 3 + African Group)
 73. Korea, Republic (own proposal + non-trade concerns)
 74. Kyrgyz Republic (transition: domestic support, market access)
 75. Latvia (transition: domestic support, market access + non-trade concerns)
 76. Lesotho (African Group)
 77. Liechtenstein (non-trade concerns)
 78. Lithuania (transition: domestic support, market access) (Joined WTO on 31 May 2001)
 79. Madagascar (African Group)
 80. Malawi (African Group)
 81. Malaysia (Cairns Group + ASEAN)
 82. Mali (own proposal + African Group)
 83. Malta (non-trade concerns)
 84. Mauritania (African Group)
 85. Mauritius (own proposal + small island developing states + non-trade concerns + African Group)
 86. Mexico
 87. Mongolia (transition: domestic support + non-trade concerns)
 88. Morocco (own proposal + African Group)
 89. Mozambique (African Group)
 90. Myanmar (ASEAN)
 91. Namibia (own proposal + African Group)
 92. New Zealand (Cairns Group)
 93. Nicaragua (developing country grouping 1, 2)
 94. Niger (African Group)

95. Nigeria (own proposal + developing country grouping 3 + African Group)
96. Norway (own proposal + non-trade concerns)
97. Pakistan (developing country grouping 1, 2, 3)
98. Paraguay (Cairns Group + MERCOSUR)
99. Philippines (Cairns Group + ASEAN)
100. Poland (own proposal + non-trade concerns)
101. Romania (non-trade concerns)
102. Rwanda (African Group)
103. Saint Kitts and Saint Nevis (small island developing states + Caricom)
104. Saint Lucia (Caricom + non-trade concerns)
105. Saint Vincent and the Grenadines (small island developing states + Caricom)
106. Sénégal (own proposal + African Group)
107. Sierra Leone (African Group)
108. Singapore (ASEAN)
109. Slovak Republic (transition: domestic support, market access + non-trade concerns)
110. Slovenia (transition: domestic support, market access + non-trade concerns)
111. South Africa (Cairns Group + African Group)
112. Sri Lanka (developing country grouping 1, 2, 3)
113. Suriname (Caricom)
114. Swaziland (own proposal + African Group)
115. Switzerland (own proposal + non-trade concerns)
116. Tanzania (African Group)
117. Thailand (Cairns Group + ASEAN)
118. Trinidad and Tobago (small island developing states + non-trade concerns)
119. Togo (African Group)
120. Tunisia (African Group)
121. Turkey
122. Uganda (developing country grouping 1, 2, 3 + African Group)
123. United States
124. Uruguay (Cairns Group + MERCOSUR)
125. Zambia (African Group)
126. Zimbabwe (developing country grouping 1, 2, 3 + African Group)

Key to the groups

ACP (African, Caribbean and Pacific Group of States) (56 WTO Members out of a total of 79):

Angola, Antigua and Barbuda, Barbados, Belize, Benin, Botswana, Burkina Faso, Burundi, Cameroon, Central African Republic, Chad, Congo, Cote d'Ivoire, Cuba, Democratic Republic of the Congo, Djibouti, Dominica, Dominican Republic, Fiji, Gabon, The Gambia, Ghana, Grenada, Guinea, Guinea-Bissau, Guyana, Haiti, Jamaica, Kenya, Lesotho, Madagascar, Malawi, Mali, Mauritania, Mauritius, Mozambique, Namibia, Niger, Nigeria, Papua New Guinea, Rwanda, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Senegal, Sierra Leone, Solomon Islands, South Africa, Suriname, Swaziland, Tanzania, Togo, Trinidad and Tobago, Uganda, Zambia, Zimbabwe

African Group (All African Members of the WTO, currently 41 countries):

Angola, Benin, Botswana, Burkina Faso, Burundi, Cameroon, Central African Republic, Chad, Congo, Congo (Democratic Republic), Côte d'Ivoire, Djibouti, Egypt, Gabon, The Gambia, Ghana, Guinea, Guinea Bissau, Kenya, Lesotho, Madagascar, Malawi, Mali, Mauritania, Mauritius, Morocco, Mozambique, Namibia, Niger, Nigeria, Rwanda, Senegal, Sierra Leone, South Africa, Swaziland, Tanzania, Togo, Tunisia, Uganda, Zambia, Zimbabwe

African Union/Group, ACP, least-developed countries (see "G-90", but with 64 WTO Members)

ASEAN (Members of WTO):
Brunei, Cambodia (WTO since October 2004), Indonesia, Malaysia, Myanmar, Philippines, Singapore, Thailand (Laos and Viet Nam are negotiating WTO Membership)

Cairns Group (19 Members since 21 November 2006, and papers e.g. G/AoA/NG/W/11, 35, 54, 93):

Argentina, Australia, Bolivia, Brazil, Canada (G/AoA/NG/W/11, 35, 93), Chile, Colombia, Costa Rica, Guatemala, Indonesia, Malaysia, New Zealand, Paraguay, Peru, Philippines, South Africa, Thailand, Uruguay

Caricom:

Antigua and Barbuda, Barbados, Belize, Dominica, Grenada, Guyana, Jamaica, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Trinidad and Tobago, Suriname

"Central American grouping": Dominican Republic, Honduras, Nicaragua and Panama, sponsored paper WT/MIN(03)/W/10 at the Cancún Ministerial Conference

Commodities Group (unofficial document JOB(05)/113):
Côte d'Ivoire, Kenya, Rwanda, Tanzania, Uganda, Zimbabwe

Cotton-4:

Benin, Burkina Faso, Chad, Mali

"Developing country grouping" = joint sponsors of:

(1) G/AoA/NG/W/13 (S&D and development box): Cuba, Dominican Republic, Honduras, Pakistan, Haiti, Nicaragua, Kenya, Uganda, Zimbabwe, Sri Lanka, El Salvador

(2) G/AoA/NG/W/14 (Green Box): Cuba, Dominican Republic, Honduras, Pakistan, Haiti, Nicaragua, Kenya, Uganda, Zimbabwe, Sri Lanka, El Salvador

(3) G/AoA/NG/W/37 + Corr.1 (market access): Cuba, Dominican Republic, El Salvador, Haiti, Honduras, Kenya, India, Nigeria, Pakistan, Sri Lanka, Uganda, Zimbabwe

"European-East Asian grouping" = joint sponsors of:

(1) JOB(03)/167: Bulgaria, Chinese Taipei, Iceland, Rep of Korea, Liechtenstein, Switzerland

(2) WT/MIN(03)/W/12: Bulgaria, Chinese Taipei, Iceland, Israel, Japan, Korea, Liechtenstein, Norway, Switzerland (See G-10)

G-10 (Currently 9 Members, since Bulgaria left):
Iceland, Israel, Japan, Rep. Korea, Liechtenstein, Mauritius, Norway, Switzerland, Chinese Taipei (See "European-East Asian grouping")

G-20 (Since 21 November 2006, 22 Members):
Argentina, Bolivia, Brazil, Chile, China, Cuba, Egypt, Guatemala, India, Indonesia, Mexico,

Nigeria, Pakistan, Paraguay, Peru, Philippines, South Africa, Tanzania, Thailand, Uruguay, Venezuela, Zimbabwe

Previously:

(1) WT/MIN(03)/W6/Add.2: Argentina, Bolivia, Brazil, Chile, China, Colombia, Costa Rica, Cuba, Ecuador, Egypt, El Salvador, Guatemala, India, Mexico, Nigeria, Pakistan, Paraguay, Peru, Philippines, South Africa, Thailand, Venezuela

(2) WT/L/559 (countries participating in the 11–12 December 2003 G-20 Ministerial Meeting): Argentina, Bolivia, Brazil, Chile, China, Cuba, Egypt, India, Indonesia, Mexico, Nigeria, Pakistan, Paraguay, Philippines, South Africa, Tanzania, Venezuela, Zimbabwe

G-33 (“friends of special products”, since 27 November 2006 understood to comprise 46 countries):

Antigua and Barbuda, Barbados, Belize, Benin, Bolivia, Botswana, China, Congo, Côte d’Ivoire, Cuba, Dominica, Dominican Republic, El Salvador, Grenada, Guatemala, Guyana, Haiti, Honduras, India, Indonesia, Jamaica, Kenya, Rep. Korea, Madagascar, Mauritius, Mongolia, Mozambique, Nicaragua, Nigeria, Pakistan, Panama, Peru, Philippines, Senegal, St Kitts and Nevis, St Lucia, St Vincent & the Grenadines, Sri Lanka, Suriname, Tanzania, Trinidad and Tobago, Turkey, Uganda, Venezuela, Zambia, Zimbabwe

G-90 (64 WTO Members of the African Union/Group, ACP and least-developed countries)

Angola, Antigua and Barbuda, Bangladesh, Barbados, Belize, Benin, Botswana, Burkina Faso, Burundi, Cambodia, Cameroon, Central African Republic, Chad, Congo, Côte d’Ivoire, Cuba, Democratic Republic of the Congo, Djibouti, Dominica, Dominican Republic, Egypt, Fiji, Gabon, The Gambia, Ghana, Grenada, Guinea (Conakry), Guinea Bissau, Guyana, Haiti, Jamaica, Kenya, Lesotho, Madagascar, Malawi, Maldives, Mali, Mauritania, Mauritius, Morocco, Mozambique, Myanmar, Namibia, Nepal, Niger, Nigeria, Papua New Guinea, Rwanda, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Senegal, Sierra Leone, Solomon Islands, South Africa, Suriname, Swaziland, Tanzania, Togo, Trinidad and Tobago, Tunisia, Uganda, Zambia, Zimbabwe

Least-developed countries (LDCs) (32 WTO Members)

Angola, Bangladesh, Benin, Burkina Faso, Burundi, Cambodia, Central African Republic, Chad, Congo, Democratic Republic of the, Djibouti, Gambia, Guinea, Guinea Bissau, Haiti, Lesotho, Madagascar, Malawi, Maldives, Mali, Mauritania, Mozambique, Myanmar, Nepal, Niger, Rwanda, Senegal, Sierra Leone, Solomon Islands, Tanzania, Togo, Uganda, Zambia

MERCOSUR:

Argentina, Brazil, Paraguay, Uruguay

“**MERCOSUR+**” = joint sponsors of:

(1) G/AoA/NG/W/38: MERCOSUR + Bolivia, Chile, Costa Rica

(2) G/AoA/NG/W/104: MERCOSUR + Bolivia, Chile, Colombia

MERCOSUR, Bolivia, Chile, Costa Rica, Guatemala, India and Malaysia sponsored proposal G/AoA/NG/W/139 on export credits

“**Non-trade concerns**” = 38 countries that sponsored note G/AoA/NG/W/36/Rev.1 (conference papers on non-trade concerns):

Barbados, Burundi, Cyprus, Czech Republic, Estonia, EU, Fiji, Iceland, Israel, Japan, Korea, Latvia, Liechtenstein, Malta, Mauritius, Mongolia, Norway, Poland, Romania, St Lucia, Slovak Republic, Slovenia, Switzerland, Trinidad and Tobago

Recent new Members (RAMS or recently acceded Members):
Albania, Armenia, Bulgaria, China, Croatia, Ecuador, FYR Macedonia, Jordan, Kyrgyz Rep., Moldova, Mongolia, Oman, Panama, Saudi Arabia, Chinese Taipei

Previously, joint sponsors of unofficial paper JOB(03)/170: Albania, Croatia, Georgia, Jordan, Moldova and Oman

“Small and vulnerable economies”:
Barbados, Bolivia, Cuba, Dominican Republic, El Salvador, Fiji, Guatemala, Honduras, Mauritius, Mongolia, Nicaragua, Papua New Guinea, Paraguay, and Trinidad and Tobago (sponsored TN/AoA/GEN/11 of 10 November 2005 and subsequent documents).

(Before that, for the September 2005 Cancún Ministerial Conference, Antigua and Barbuda, Barbados, Belize, Bolivia, Cuba, Dominica, Dominican Republic, El Salvador, Fiji, Grenada, Guatemala, Guyana, Honduras, Jamaica, Kyrgyz Rep, Maldives, Mauritius, Mongolia, Nicaragua, Paraguay, Papua New Guinea, Solomon Islands, Sri Lanka, St. Kitts and Nevis, St. Lucia, St. Vincent and the Grenadines, Trinidad and Tobago sponsored WT/MIN(05)/22 and addenda. All are ACP Members except Bolivia, El Salvador, Guatemala, Honduras, Kyrgyz Rep, Maldives, Mongolia, Nicaragua, Paraguay, Sri Lanka)

“Small island developing states” (SIDS):
Barbados, Cuba, Dominica, Jamaica, Mauritius, St Kitts and Nevis, St Lucia, St Vincent and the Grenadines, Trinidad and Tobago

Recently-acceded Members (RAMs):
Albania, Armenia, Bulgaria, China, Croatia, Ecuador, FYR Macedonia, Jordan, Kyrgyz Rep., Moldova, Mongolia, Oman, Panama, Saudi Arabia, Chinese Taipei

Previously “Transition Group”, joint sponsors of:

(1) *G/AoA/NG/W/56* (domestic support): Albania, Bulgaria, Croatia, the Czech Republic, Georgia, Hungary, the Kyrgyz Republic, Latvia, Lithuania, Mongolia, Slovak Republic, Slovenia

(2) *G/AoA/NG/W/57* (market access): Bulgaria, Czech Republic, Estonia, Georgia, Hungary, Kyrgyz Republic, Latvia, Slovak Republic, Slovenia, Croatia, Lithuania

Tropical products group:
Bolivia, Bol. Rep. Venezuela, Colombia, Costa Rica, Ecuador, El Salvador, Honduras, Guatemala, Nicaragua, Panama, Peru

Annex V

**Interview of Roberto Azevedo, the former chief of the Brazilian Mission at WTO in Geneva
(16 October 2004) in Brazilian Ministry of Foreign Affairs, Brasilia**

Questions:

1. Contact with the Brazilian Association of Cotton Producers ABRAPA and with other lawyers involved in the cases.
2. Idiosyncrasies that deserve to be mentioned about the *US – Subsidies on Cotton*.
3. Major difficulties about the dispute.
4. Procedural and legal difficulties during the first part of the case: division of procedures because of the Peace Clause, delays on deadlines and others.
5. Legal perspectives for Appellation.
6. Impacts of the Case in the agricultural framework being negotiated in the Doha Round. Factors of Success.

Comments of Mr. Azevedo.

Roberto Azevedo and Nilo Dytz Filho worked in the dispute. Mr. Azevedo stated Itamaraty (Brazilian Diplomatic Department) had an important decisional role, but CAMEX (Brazilian Department of Foreign Trade of Ministry of Development, Industry and Foreign Trade) also contributed because it was responsible for the initiation of the dispute when consultation started in the end of 2002.

Itamaraty had a first meeting with the lawyers to define strategies and tactics of the case itself. For this reason the material on econometrics produced by Prof. Daniel Sumner was used.

The Itamaraty's team worked in the draft of the petitions making comments according to the legal strategy defined together with the lawyers hired by the Brazilian government. The Brazilian diplomats also collected data and harmonized information received from Prof. Sumner and from lawyers.

One of the strategies was to prove the interference of agricultural subsidies in the determination of cotton price, which is a commodity negotiated in stock markets. In this matter,

one idiosyncrasy can be mentioned. An intern from the law firm hired by the Brazilian government was able to get information about American subsidies for cotton that was not public.

There was no other idiosyncrasy related with the fact the case was against the US government. On the contrary, it was easier to get information about American programs if compared to cases against other countries. According to Mr. Azevedo, American information was transparent.

Regarding Doha agricultural negotiations, the Itamaraty's team that work with WTO disputes had one conversation with the team that negotiates agriculture in the Doha Round to avoid that challenged measures in the panel were discussed in the negotiations. In this way the negotiations were facilitated because controversial subjects in the Doha agricultural negotiations were reduced.

A success factor was the choice of this specific case about cotton (because there was substantial information about the levels of subsidy that were higher than it was allowed by the *AoA*) and the quality of the lawyers hired by the Itamaraty that worked in the case. The studies of Prof. Sumner that made the econometrics were also extremely relevant. The American petitions were predictable.