

UNITED STATES – SUBSIDIES ON UPLAND COTTON:

Recourse to Article 21.5 of the DSU by Brazil

(WT/DS267)

**U.S. Comments on the Answers of Brazil
to the Second Set of Questions from the Panel**

April 24, 2007

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167	U.S. Export Sales Weekly Export Performance Indicator for Week Ending 4.12.2007, available at http://www.fas.usda.gov/esrquery/esrpi.aspx .
168	NASS March 2007 Cotton Ginnings Report
169	N.Y. Futures After Issuance of Planting Intentions Report

1. In its answers to the second set of questions from the Panel, Brazil has reasserted many of the same unfounded arguments presented in its earlier submissions, which the United States has already addressed and rebutted. Many of Brazil's answers to questions also repeat the same information. The United States does not intend to resubmit all of these U.S. arguments in response. Rather, for the convenience of the Panel, the United States first offers one general comment regarding Brazil's answers to each major section of the Panel's questions. The United States then proceeds to address those aspects of Brazil's answers that are either new or call for further comment. Where possible, the United States refers the Panel to its prior submissions where Brazil's arguments have been addressed.

2. To the extent the United States does not address a particular answer or a particular aspect of an answer, this is not intended as – and should not be understood to be – agreement with Brazil's position.

I. GENERAL COMMENTS REGARDING BRAZIL'S ANSWERS

A. BRAZIL HAS NO BASIS TO CHALLENGE MEASURES THAT WERE NEITHER ORIGINAL MEASURES SUBJECT TO ANY FINDING OF WTO-INCONSISTENCY OR DSB RECOMMENDATIONS AND RULINGS NOR MEASURES TAKEN TO COMPLY WITH ANY RECOMMENDATIONS AND RULINGS¹

3. Brazil repeats in its answers to Questions 44 to 46 the incorrect argument that it is entitled to renew in this "compliance" proceeding under Article 21.5 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") claims against measures (a) that were never found to be WTO-inconsistent and were never subject to any DSB recommendations and rulings; and (b) that are not measures taken to comply with any recommendations and rulings.² These measures include the GSM 102 export credit guarantees in respect of exports of pig meat and poultry meat. They also include the marketing loan and counter-cyclical payment programs and payments made under the program in years beyond MY 1999-2002. Brazil's arguments continue to be unavailing.

1. Neither GSM 102 guarantees in respect of exports of pig meat and poultry meat nor Brazil's claims with respect to them are within the scope of this proceeding

¹ The United States does not submit comments regarding Brazil's claims in respect of compliance in past periods as none of Brazil's answers to the second set of questions relate to that issue. For the U.S. arguments in respect of those claims, the United States respectfully refers the Panel to the U.S. First Written Submission, paras. 49-56, U.S. Rebuttal Submission, paras. 64-71, U.S. Answers to Parts A-C of First Set of Panel Questions, paras. 45-46, U.S. Comments on Brazil's Answers to First Set of Panel Questions, paras. 104-111, and U.S. Answers to Second Set of Panel Questions, paras. 54-61.

² See Brazil Answers to Second Set of Questions, paras. 1-35.

4. Brazil's assertion of an "entitlement" to make a claim against GSM 102 guarantees in respect of exports of pig meat and poultry meat rests on two untenable grounds. First, Brazil asserts erroneously that *any* changed measure may be challenged in a compliance proceeding regardless of whether it was "taken to comply" with any recommendations and rulings of the DSB.³ And, second, Brazil asserts that a complaining party may renew in a compliance proceeding any claims that were not "definitively resolved" in the original proceeding.⁴ Neither proposition finds support in the DSU.

5. Contrary to Brazil's assertions, the test of whether a measure is properly within the scope of an Article 21.5 compliance proceeding is not simply whether it has changed since the original proceeding. That would effectively write out of Article 21.5 the requirement that the measure be "taken to comply" with the DSB's recommendations and rulings. Rather, under the express terms of Article 21.5, the touchstone of what is and is not a "measure taken to comply with the recommendations and rulings" of the DSB is – necessarily – the DSB's recommendations and rulings. Where the DSB's recommendations and rulings distinguish between different components of a measure or different measures, that distinction is determinative for purposes of the compliance proceeding as well.

6. Here, the DSB's recommendations and rulings clearly distinguish "export credit guarantees under the GSM 102, GSM 103 and SCGP export credit guarantee programmes . . . in respect of exports of upland cotton and other unscheduled agricultural products supported under the programmes, and in respect of one scheduled product (rice)"⁵ from other export credit guarantees under those programs. As Brazil's response to Question 44 confirms, this distinction goes to which *measures* were found to be WTO-inconsistent (*i.e.*, which measures the United States was obligated to bring into compliance with its obligations under Articles 10.1 and 8 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement*). The question for this compliance Panel, then, is whether Brazil has demonstrated either that the United States has (a) not brought those measures (export credit guarantees in respect of rice and unscheduled products) into conformity with the DSB's recommendations and rulings or (b) that those measures – as modified – are inconsistent with the provisions of the WTO Agreement cited by Brazil.⁶

7. Brazil has attempted to obscure this distinction by insisting variously that (a) the original

³ See *e.g.*, Brazil Answers to Second Set of Questions, para. 6, 34.

⁴ See *e.g.*, Brazil Answers to Second Set of Questions, para. 7.

⁵ *Upland Cotton (Panel)*, para. 8.1(d) (emphasis added). This is because the original panel found that Brazil had only made its case under Articles 10.1 and 8 of the *Agreement on Agriculture* and Articles 3.1(a) and 3.2 of the *SCM Agreement* with respect to export credit guarantees provided in respect of exports of rice and unscheduled products.

⁶ There can be no presumption that the U.S. measures taken to comply are inconsistent with its WTO obligations; the burden is on Brazil to prove inconsistency.

panel's findings were made with respect to the GSM program as a whole⁷ and that guarantees thereunder are not even "measures" for purposes of WTO dispute settlement⁸, (b) that it is Brazil's *claims* and not the measures challenged that are "product specific;"⁹ (c) that the United States has made changes across the entire GSM 102 program including with respect to export credit guarantees in respect of exports of pig meat and poultry meat,¹⁰ and (d) and that the GSM 102 program applies in the same way regardless of what products are involved.¹¹ As the United States has explained,¹² however, not only are certain of these assertions wrong, they do not alter the conclusion that GSM 102 export credit guarantees in respect of exports of pig meat and poultry meat are not within the scope of this proceeding.

2. The marketing loan and counter-cyclical payment programs, payments made thereunder after MY 2002, and Brazil's claims in respect of those measures are outside the scope of this proceeding

8. In its response to Question 45, Brazil continues to press the Panel impermissibly to

⁷ As the United States has explained, this argument is inconsistent with Brazil's prior arguments and the original panel's resolution of Brazil's claims. See U.S. Comments on Brazil's Answers to First Set of Panel Questions, paras. 12-15. This even contradicts Brazil's own clarification in its rebuttal submission that "*Brazil does not assert that the GSM 102 program itself circumvents the United States' export subsidy commitments, within the meaning of Article 10.1 of the Agreement on Agriculture.*" Brazil Rebuttal Submission, para. 378 (emphasis added).

⁸ See, e.g., Brazil Responses to Panel Section A-C Questions, para. 29. This argument is at odds with Brazil's arguments elsewhere that an *a contrario* reading of item (j) would prevent a Member from challenging specific export credit guarantees (i.e., as opposed to the export credit guarantee *programs* generally). See U.S. Comments on Brazil's Answers to First Set of Panel Questions, paras. 10-11. If specific guarantees cannot even constitute "measures," as Brazil now asserts, Brazil's complaints about being able to make claims against specific guarantees would be entirely moot. Brazil's argument is also inconsistent with the clarification by the Appellate Body that a "measure" for purposes of WTO dispute settlement may encompass "[i]n principle, any act or omission attributable to a WTO Member. . . ." *United States – Corrosion-Resistant Steel (AB)*, para. 81.

⁹ Calling Brazil's claims "product-specific" does not change the fact that only particular guarantees – those provided in respect to the particular "product" at issue – are the subject of the claims. Where those guarantees were not the subject of any DSB recommendations and rulings and are not measures taken to comply with any DSB recommendations and rulings – as in the case of the GSM 102 export credit guarantees in respect of exports of pig meat and poultry meat – there is no basis for a claim to be considered with respect to them in a DSU Article 21.5 proceeding. See U.S. Comments on Brazil's Answers to First Set of Panel Questions, paras. 16.

¹⁰ See e.g., Brazil Answers to Second Set of Panel Questions, para. 6. As the panel in *EC – Bed Linen (21.5)* recognized the mere fact that improvements have been made to more than just the original measures subject to findings of WTO-inconsistency and DSB recommendations and rulings does not render all changed measures "measures taken to comply." See U.S. Answers to Second Set of Panel Questions, paras. 1-16 (discussing *EC – Bed Linen (21.5) (Panel)*, paras. 6.9-6.22).

¹¹ See e.g., Brazil Answers to Second Set of Panel Questions, para. 4. Contrary to Brazil's assertions, the U.S. argument is not premised on the assumption "that different ECG measures apply to different products." Brazil Answers to Second Set of Panel Questions, para. 4. As the United States has explained, this is irrelevant to the U.S. arguments.

¹² U.S. First Written Submission, paras.24-30, U.S. Rebuttal Submission, paras. 10-15, U.S. Answers to Parts A-C of First Set of Panel Questions, paras. 17-26, U.S. Comments on Brazil's Answers to First Set of Panel Questions, paras. 8-44, and U.S. Answers to Second Set of Panel Questions, paras. 1-16 and 42-48.

expand the scope of this compliance proceeding to include claims against the marketing loan and counter-cyclical payment programs and payments made thereunder in periods after MY 2002. Brazil's arguments turn on its own pronouncements that the original panel did in fact find the Step 2, marketing loan, and counter-cyclical payment programs to be causing "present" serious prejudice and that it similarly found payments allegedly "mandated" to be made thereunder in MY 2003-2007 to be causing "present" serious prejudice (though, of course, such payments had not even been made as of the time the matter was referred to the original panel). These pronouncements are flatly contradicted by the facts and the express language of the original panel report.

9. Brazil's approach in Question 45 – as it has been throughout this proceeding – consists of cherry-picking individual sentences of the panel report and imposing upon them a strained reading that is neither supported by the context nor consistent with the most basic principles of WTO dispute settlement (e.g., that a panel cannot make the claim for a complaining party, let alone make claims never presented by a complaining party). As the United States has explained, there is no merit to these arguments.¹³

10. In fact, it is remarkable that, in its response to Question 45 from the Panel, Brazil accuses the United States of "mischaracteriz[ing] the original panel's findings from beginning to end."¹⁴ Not only is this untrue, but the irony of the accusation is that Brazil has never even attempted to reconcile its arguments with the "original panel's findings from beginning to end." So, for example, Brazil has never explained what legal basis this Panel has for ignoring the original panel's *actual* conclusion on present serious prejudice:

In conclusion, in light of all of these considerations, we find that the effect of the mandatory, price contingent United States subsidies at issue – *that is*, marketing loan programme *payments*, user marketing (Step 2) *payments* and MLA *payments* and CCP *payments* – is significant price suppression in the same world market for upland cotton in the period MY 1999-2002 within the meaning of Articles 6.3(c) and 5(c) of the SCM Agreement.¹⁵

This conclusion *on its face* contradicts Brazil's assertion that "the United States . . . wrongly assumes that 'U.S. subsidies' does not include the legislative and regulatory provisions – the subsidy programs – mandating the subsidy payments."¹⁶ The language confirms that the United States has not *assumed* – let alone *wrongly* assumed – what the "U.S. subsidies" are, as Brazil charges.

¹³ U.S. First Written Submission, paras. 31-48, U.S. Rebuttal Submission, paras. 16-63, U.S. Answers to Parts A-C of First Set of Panel Questions, paras. 27-44, U.S. Comments on Brazil's Answers to First Set of Panel Questions, paras. 45-103, and U.S. Answers to Second Set of Panel Questions, paras. 17-41.

¹⁴ Brazil Answers to Second Set of Panel Questions, para. 12.

¹⁵ *Upland Cotton (Panel)*, para. 7.1416.

¹⁶ Brazil Answers to Second Set of Panel Questions, para. 13.

11. To the contrary, as the original panel clearly states, the “United States subsidies at issue” . . . [are] marketing loan programme *payments*, user marketing (Step 2) *payments*, MLA *payments*, and. . . CCP *payments*.” There is no other way to understand the language in between the dashes in the conclusion or the fact that the original panel uses the introductory phrase “that is” – a phrase used for clarification of what a term means – to explain that the “subsidies at issue” are marketing loan programme *payments*, user marketing (Step 2) *payments*, MLA *payments*, and counter-cyclical *payments*. Brazil has never reconciled its theory – that the “subsidies at issue” include the programs providing for these payments – with this language or with the scores of other clear indications by the original panel that the subsidies subject to its “present” serious prejudice examination were payments made in MY 1999-2002 under, *inter alia*, the Step 2, marketing loan, and counter-cyclical payment program.

12. Nor has Brazil offered any credible explanation for:

- How the original panel could have made a finding of *present* serious prejudice against either the Step 2, marketing loan, and counter-cyclical payment programs or payments allegedly “mandated” to be made thereunder in MY 2003-2007 when it did not recognize Brazil as even presenting a *claim* of “present” serious prejudice with respect to either group of measures.¹⁷
- Why the original panel identified only “user marketing (Step 2) *payments* to domestic users and exporters; marketing loan programme *payments*; PFC *payments*; MLA *payments*; DP *payments*; CCP *payments*; crop insurance *payments*; and cottonseed *payments*”¹⁸ as the “challenged measures” that were alleged to be the “subsidies” for purposes of Brazil’s “present” serious prejudice claim. The panel only found that those measures constituted subsidies within the meaning of Articles 1 and 2 of the *SCM Agreement*.¹⁹ The panel did not conduct *any* assessment as to whether the statutory/regulatory provisions authorizing these payments were also “subsidies.”

¹⁷ The United States recalls that the panel set out the claims presented by Brazil as follows: (a) claims of “present” serious prejudice with respect to “U.S. subsidies provided during MY 1999-2002”; (b) claims of threat of serious prejudice with respect to “U.S. subsidies mandated to be provided in MY 2003-2007;” and (c) *per se* claims of threat of serious prejudice against “selected provisions of the FSRI Act of 2002 and the ARP Act of 2000” providing for these subsidies, to the extent relevant to upland cotton, and their implementing regulations. *Upland Cotton (Panel)*, para. 3.1(vi) – 3.1(viii). The original panel did *not* identify a “present” serious prejudice claim under Article 5(c) and 6.3(c) of the *SCM Agreement* as one of the claims “concerning selected provisions of the FSRI Act of 2002 and the ARP Act of 2000.” Nor did the original panel identify “selected provisions of the FSRI Act of 2002 and the ARP Act of 2000” as part of the measures subject to Brazil’s claims of “present” serious prejudice under Articles 5(c) and 6.3(c) of the *SCM Agreement*.

¹⁸ *Upland Cotton (Panel)*, para. 7.1120. The original panel ultimately found that these constituted “subsidies” within the meaning of Article 1 of the *SCM Agreement* because they were “financial contributions” (mostly in the form of “grants”) conferring a “benefit.” *Upland Cotton (Panel)*, paras. 7.1112-7.1120.

¹⁹ *Upland Cotton (Panel)*, para. 7.1112-7.1120.

- How the original panel could have made findings of WTO-inconsistency with respect to the Step 2, marketing loan, and counter-cyclical payment programs or future payments allegedly “mandated” to be made under the programs without addressing the extensive arguments that the parties made, and without making any of the factual findings that *Brazil* conceded would be necessary to support an affirmative finding of WTO-inconsistency in respect of those measures.²⁰

13. And Brazil has not addressed the other clear textual signals that – consistent with the claims presented to it – the original panel’s findings of “present” serious prejudice were made with respect to payments made in MY 1999-2002. This includes:

- The fact that the original panel’s prohibited subsidy-related conclusions and recommendations regarding the Step 2 program, *as such*, expressly refer to “section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to exporters of upland cotton”²¹ and “section 1207(a) of the FSRI Act of 2002 providing for user marketing (Step 2) payments to domestic users of upland cotton.”²² If the conclusions regarding “present” serious prejudice in paragraphs 8.3(d) and 8.1(g)(i) of the original panel report also pertained to the Step 2 program, *as such*, together with the marketing loan program and counter-cyclical payment program, the panel would certainly have included the same specific kind of reference, rather than a reference to “user marketing (Step 2) payments..”
- The fact that in Section VII:D of the Panel Report, dealing with the evaluation of domestic support measures under Article 13 of the *Agreement on Agriculture*, the original panel expressly stated that, “[i]n this Section of our report, the Panel will consider the current programmes ‘as applied’ and ‘as such’ together. Therefore, references to marketing loan programme, user marketing (step 2), direct, counter-cyclical and crop insurance ‘payments’ include the legislative and regulatory

²⁰ For example, Brazil conceded in the original proceeding that “[i]t is established under WTO law that a Member can only challenge measures of another Member *per se* if such measures mandate a violation of the WTO Agreement.” Brazil First Submission in Original Panel Proceeding, para. 244 (citing *US – 1916 Act (AB)*, para. 88). Thus, in the case of its claims against the challenged programs, *per se*, Brazil asked the Panel “to find that the mandatory provisions of the 2002 FSRI Act and the 2000 ARP Act together with their implementing regulations, as listed above, *cannot be applied in a WTO consistent manner.*” Brazil’s 9 September 2003 Further Submission, para. 435-436. Explaining what this would mean in the context of this dispute, Brazil argued “[f]irst, the Panel needs to evaluate whether the U.S. subsidies will *necessarily threaten* to cause serious prejudice at price levels below the trigger prices of the U.S. subsidies. Second, the Panel needs to consider whether the U.S. subsidies threaten to cause serious prejudice *even at price levels at which only crop insurance subsidies and direct payments are made.*” Brazil’s September 9, 2003 Further Submission, para. 426 (emphasis added). The Panel neither conducted the requested evaluations, nor made any findings along the lines requested by Brazil.

²¹ See *Upland Cotton (Panel)*, paras. 8.3(b) and 8.1(e).

²² See *Upland Cotton (Panel)*, paras. 8.3(c) and 8.1(f).

provisions authorizing those payments unless otherwise indicated.”²³ No similar statement can be found in Section VII:G, which is the section including the original panel’s analysis of the effects of the subsidies alleged to be causing serious prejudice. In fact, the original panel in Section VII:G clearly distinguishes payments from provisions providing for those payments. Nor is there any similar statement made in connection with the recommendation in paragraph 8.3(d) of the panel report (or paragraph 8.1(g)(i), which contains the conclusion on actionable subsidies to which the recommendation relates).

- The panel’s clarification that it was not precluded from considering whether production flexibility contract and market loss assistance *payments* were causing “present” serious prejudice even though the legislative and regulatory provisions authorizing those payments had expired even before Brazil made its request for consultations.²⁴ If the original panel’s findings with respect to “payments” – and the DSB’s recommendations and rulings on the basis thereof – were to be understood to automatically refer also to the programs authorizing those payments, as Brazil urges, the recommendation with respect to “MLA payments” in the panel’s “present” serious prejudice conclusion would necessarily be a recommendation also with respect to the “MLA program” as such (an expired measure). This would be inconsistent with the original panel’s express clarification that it was not making any findings of WTO-inconsistency or any recommendations and rulings with respect to expired programs, as such²⁵ as well as with the Appellate Body’s subsequent clarification that “there [is] an obvious inconsistency” between a finding that a measure has expired and a “subsequent recommendation that the . . . DSB request the United States to bring the [expired measure] into conformity with its WTO obligations.”²⁶

14. In short, Brazil has not – and cannot – reconcile its own arguments to the “the original panel’s findings from beginning to end.”²⁷ Brazil’s does not offer any coherent interpretation of the original panel report that addresses and takes into account all of the facts discussed above and in the prior U.S. submissions. Simply ignoring the facts or making accusations that the United States is “mischaracteriz[ing] them” does not allow Brazil to overcome that fatal deficiency. It remains, therefore, that Brazil’s claims against the marketing loan and counter-

²³ *Upland Cotton (Panel)*, para. 7.337(ix), n. 466.

²⁴ *Upland Cotton (Panel)*, para. 7.108 (“The Panel notes that Brazil pursues claims only in respect of the subsidies and domestic support provided under the expired programmes and authorizing legislation, in other words, *the payments themselves*. Brazil does not seek any relief in respect of the PFC and MLA programmes or authorizing legislation ‘as such.’ Therefore, the Panel only considers whether the payments are within its terms of reference.”) (italics added).

²⁵ *Upland Cotton (Panel)*, para. 7.111.

²⁶ *Upland Cotton (AB)*, para. 272 (citing *U.S. – Certain EC Products (AB)*, paras. 81-82).

²⁷ Brazil Answers to Second Set of Panel Questions, para. 12.

cyclical payment programs and any payments made under the programs post-MY 2002 are outside the scope of this proceeding.

B. MARKETING LOAN AND COUNTER-CYCLICAL PAYMENT PROGRAMS ARE NOT CAUSING ANY PRESENT “SIGNIFICANT” PRICE SUPPRESSION WITHIN THE MEANING OF ARTICLES 5(C) AND 6.3(C) OF THE *SCM AGREEMENT*

15. For the reasons set out above and in the prior U.S. submissions, Brazil’s claims of “present” serious prejudice under Articles 5(c) and 6.3(c) of the *SCM Agreement* against the marketing loan and counter-cyclical payment programs and/or any present payments thereunder are not within the scope of this proceeding. Were they to have been within the scope, they would nonetheless fail because they are bereft of a basis in the facts.

16. Indeed, a substantial part of Brazil’s responses to the Panel’s Questions 51 and 62-74 are devoted to attempts to explain away this failing. Brazil complains, on the one hand, that it should not be required to provide “direct evidence of what would actually happen to U.S. acreage, production, exports, and world prices”²⁸ without marketing loan and counter-cyclical payments and it complains, on the other, that the United States has “ignore[d] the hundreds of exhibits and circumstantial evidence presented by Brazil.”²⁹ Both assertions are baseless.

17. Brazil – as the complaining party – bears the burden of proving its claims with evidence and arguments that actually *support the claim for which they are offered*. It has not done so. Further, in observing this, the United States has not “ignored” any argument or exhibit submitted by Brazil. To the contrary, the United States has painstakingly examined and addressed – over the course of two written submission, the presentation before the Panel, three set of responses to questions from the Panel, comments on Brazil’s “oral” presentation to the Panel, and now two sets of comments on answers – every argument made by Brazil and demonstrated that these do not, individually or collectively, support Brazil’s claims of “significant” price suppression.³⁰

18. ***Brazil’s assertions about the removal of the Step 2 program are unsubstantiated, internally contradictory, and inconsistent with arguments made by Brazil in the original proceeding:*** Brazil’s claims are premised on the assertion that removal of the Step 2 program has not removed the adverse effects of the package of payments found by the original panel to be

²⁸ Brazil Answers to Second Set of Panel Questions, para. 91.

²⁹ Brazil Answers to Second Set of Panel Questions, para. 90.

³⁰ In fact, if the United States were in fact “ignor[ing]” Brazil’s arguments, one can only wonder why Brazil has repeatedly attempted over the course of this proceeding to attempt to cut U.S. opportunities for response: for example, arguing at the start of the proceeding that the United States should be given no more than two weeks to respond to Brazil’s nearly 200-page first written submission and; arguing that the United States should not be permitted to address Brazil’s contingent “threat” claim in its rebuttal submission; arguing that the United States should be given no opportunity to respond to Brazil’s unsolicited third written submission submitted under the guise of an “exhibit” to Brazil’s “oral” presentation; and in its latest attempt to obtain an unfair procedural advantage, arguing against the grant of any additional time for submission of these comments.

causing “present” serious prejudice. However, Brazil’s assertions about the effects of removing the Step 2 program are unsubstantiated, internally contradictory, inconsistent with arguments made by Brazil in the original proceeding, and contradicted by the empirical evidence.³¹

19. Thus, for example, having proclaimed to the original panel that “it is difficult to imagine how a subsidy could be *more* of an export subsidy than the Step 2 export provisions” and that “[the program] plays an important role in stimulating and maintaining the present record high U.S. upland cotton world export market share,”³² Brazil has no basis now to allege that “removal of the Step 2 program does [not] result in any significant or long-term reduction of U.S. exports.”³³ The United States notes the irony in Brazil’s assertion here that a “long-term” assessment of the effects of the removal of the Step 2 program is appropriate while in its analysis of the marketing loan and counter-cyclical payment program it insists that “the assessment is necessarily of a short-term, not a long-term nature.”³⁴ This is yet further evidence that Brazil’s positions on such fundamental questions as the appropriate analysis under the *SCM Agreement* shift simply depending on its preferred outcome. Moreover, the United States notes that Brazil’s asserted bases for this assertion do not withstand scrutiny.

20. Indeed, while Brazil attempts to assert as evidence a statement by a National Cotton Council (“NCC”) representative that in MY 2007, “NCC sees U.S. exports recovering to 16.22 million bales as foreign mill use increases,” Brazil fails to quote for the Panel the statement immediately prior to this one in which the same representative notes that:

the 2006 marketing year is the first of the post-Step 2 era, and the impact on exports has been evident. Through mid-January, export commitments of upland cotton totaled roughly 6 million bales. This time a year ago, total commitments had surpassed 10 million bales.³⁵

The United States recalls Brazil’s assertion that in assessing the effects of payments “the views of their recipients constitute particularly relevant evidence.”³⁶ Brazil would presumably attach similar importance to the NCC statement it neglected to cite.

21. In any event, the possibility of an increase in the export volume in MY 2007 in *absolute* terms does not change the analysis regarding the effects of removing the Step 2 program. As the

³¹ The full U.S. arguments in this respect are set out at U.S. First Written Submission, paras. 149-195, U.S. Rebuttal Submission, paras. 175-214, and U.S. Oral Statement, paras. 54-59.

³² Brazil’s Rebuttal Submission to the Panel Regarding the “Peace Clause” and Non-Peace Clause Related Claims,” para. 128 (22 August 2003) (emphasis in original).

³³ Brazil Answers to Second Set of Panel Questions, para. 90.

³⁴ Brazil Answers to Second Set of Panel Questions, para. 131.

³⁵ “US Cotton Industry To Face Challenges In Global Market,” 2006 AgWeb.com (Exhibit BRA-679).

³⁶ Brazil Answers to Second Set of Panel Questions, para. 48.

United States explained in its rebuttal submission,³⁷ such factors as China's import needs may have contributed in part to the decline in the level of U.S. exports as of August, 2006. And as there are changes in those factors, there may well be effects in the level of U.S. exports. However, those factors do not account for the entire decline. Thus, for example, primarily in connection with the pending release of import quota by China,³⁸ there have been recent purchases of some 795,800 running bales of U.S. cotton.³⁹ This represents a marketing-year high. Yet, even with these purchases, total export commitments, both sales and shipments, are 31% and 15% below last year's total and the 5-year average, respectively.⁴⁰ The fact that U.S. export volume may recover somewhat in the future, thus, does not suggest that export levels would not have been even higher had the Step 2 program been in effect.

22. In the face of such empirical data at odds with its assertions (for purposes of this proceeding) about the alleged effects of eliminating the Step 2 program, Brazil urges the Panel, in its response to Question 74, to consider MY 2005 – *a year in which Step 2 payments were still in effect* – as the relevant period for purposes of its analysis of the effects of removal of the Step 2 program. Presumably, the Panel would then have to accept Brazil's assertions (for purposes of this proceeding) about what the effects of that program would or would not have been in that year rather than relying on the actual evidence thereof. Neither this suggestion by Brazil nor its unsubstantiated assertions about the effects of removing the Step 2 program may be credited.

23. ***Brazil does not show that marketing loan and counter-cyclical payments cause "present" serious prejudice:*** Citing the original panel, Brazil argues that "an examination of the 'effects'" of the challenged measures "cannot be conducted in the abstract."⁴¹ Yet, in support of its claims, Brazil repeatedly suggests that, even without considering the existing market conditions (or conducting any assessment of what these were likely to be) the original panel somehow found marketing loan and counter-cyclical payments to be causing significant suppression of world market prices today.⁴² Similarly, it makes generic assertions about impacts on wealth and risk aversion that – if credited – would effectively preclude *any* payment to farmers no matter what their form and no matter how minimal their impact on planting, production, exports, and prices.⁴³

24. Brazil's claim cannot properly rest on these bases. For one, the original panel did not

³⁷ U.S. Rebuttal Submission, paras. 206-213.

³⁸ "China: Cotton import quotas of 1.5mn tons to be issued," available at www.fibre2fashion.com (April 24, 2007) (Exhibit US-165).

³⁹ U.S. Export Sales for Week Ending 4.12.2007, available at www.fas.usda.gov/export-sales/cottfax.htm (Exhibit US-166).

⁴⁰ U.S. Export Sales Weekly Export Performance Indicator for Week Ending 4.12.2007, available at <http://www.fas.usda.gov/esrquery/esrpi.aspx> (Exhibit US-167).

⁴¹ Brazil Answers to Second Set of Panel Questions, para. 10 (citing *Upland Cotton (Panel)*, para. 10).

⁴² See e.g., Brazil Answers to Second Set of Panel Questions, paras. 45, 53-55, 94, 99.

⁴³ See e.g., Brazil Answers to Second Set of Panel Questions, paras. 49, 55, 94.

find that marketing loan and counter-cyclical payment *programs* caused significant price suppression in MY 1999-2002. Therefore, Brazil is incorrect to assert – in response to Question 69, for example – that it could prove significant price suppression in this proceeding merely by asserting⁴⁴ that payments were made under those programs over the course of the FSRI Act and that “[t]he world market for upland cotton identified by the original panel still functions on the same basis as found by the original panel.”⁴⁵ The original panel’s finding of “present” serious prejudice related to the effects of an entirely different set of measures (*payments* not only under the marketing loan and counter-cyclical payment programs but also under the Step 2 program) made in a different time period (MY 1999-2002) and under substantially different market conditions. There have been many changes since that time. These include not only the removal of the Step 2 program but many other factors, for example production-related technological changes that have had dramatic effects on the cost structure of U.S. upland cotton farming (as well as farmers in other countries, such as India) and shifts in patterns of world trade in upland cotton – shifts that are so significant that even the basis for Brazil’s asserted “world market price” (the A-Index) has had to be changed (from a Northern Europe basket of quotes to a Far Eastern basket of quotes).

25. The original panel did not – and could not – have taken these factors into account in assessing the “present” effects of the different package of measures at issue in the original proceeding. And, in fact, it is precisely because the original panel could *not* predict what these changes might be (for example, if the United States were to modify the statutory and regulatory provisions providing for Step 2, marketing loan, or counter-cyclical payments in order to implement the Panel’s findings), or foresee what effect the challenged measures might have under such changed factual circumstances, that it declined to make any “threat” finding against either future payments or the marketing loan and counter-cyclical payment programs as such.

26. In addition, as explained in the U.S. comments regarding Question 62, Brazil’s attempts to indict support to agricultural producers simply on the basis it contributes to the “wealth” of producers and may render them less “risk averse” in their production decisions cannot be credited. If Members had agreed that no domestic support could be provided to agricultural producers, the *Agreement on Agriculture* could have been a great deal shorter. The drafters could simply either have inserted one provision either in that agreement or the *SCM Agreement* stating that “no Member shall provide payments to any producer of any commodity” as this, *inevitably*, contributes to the “wealth” of the producer and, as such, may also render him less risk averse. No such provision exists in either agreement because Members have not agreed to such a prohibition.⁴⁶

⁴⁴ These are assertions by Brazil, not “undisputed facts,” as it has stated. Brazil Answers to Second Set of Panel Questions, para. 95.

⁴⁵ Brazil Answers to Second Set of Panel Questions, para. 94.

⁴⁶ To the contrary, there is one agriculture-specific actionable subsidy provision in the *SCM Agreement* – Article 6.3(d) of the *SCM Agreement* – and that falls far short of a blanket prohibition on any subsidy that increases producer wealth and renders them less risk averse.

27. What the United States finds instead is clear recognition in the *Agreement on Agriculture* and *SCM Agreement* that domestic support to producers of a commodity may have effects that lie anywhere in a range from “no or at most minimal, trade-distorting effects” to more substantial effects that may implicate the reduction commitment obligations in the *Agreement on Agriculture* but are not of the type to render the domestic support an “actionable subsidy” under the *SCM Agreement*, to the kinds of serious effects on trade identified under Articles 5 and 6 of the *SCM Agreement*. It is only the latter – “adverse effects” to the interests of another Member – that are disciplined under the *SCM Agreement*. Whether or not a Member may *challenge* a measure under the *SCM Agreement* has no bearing on whether it can establish a breach of Articles 5(c) and 6.3(c). It can only do the latter where it proves that “the effect” of a measure found to be a “subsidy” is “significant price suppression” within the meaning of Article 5(c) and 6.3(c) of the *SCM Agreement*.

28. As the United States has demonstrated,⁴⁷ none of the allegedly “abundant and diverse evidence” that Brazil asserts in its answers to questions or any of its prior submissions proves that this is “the effect” of the marketing loan and counter-cyclical payments. What the substantial evidence shows, instead, is that any effects of marketing loan and counter-cyclical payments on U.S. planting, production, exports or world market prices of upland cotton are minimal and not subject to discipline under Articles 5 and 6 of the *SCM Agreement*.

C. THE EFFECT OF THE MARKETING LOAN AND COUNTER-CYCLICAL PAYMENT PROGRAMS IS NOT ANY “PRESENT” INCREASE IN THE U.S. SHARE OF THE WORLD MARKET FOR UPLAND COTTON WITHIN THE MEANING OF ARTICLES 5(C) AND 6.3(D) OF THE *SCM AGREEMENT*

29. Even though Brazil has admitted that “U.S. *share* of world production . . . stayed relatively stable” over the entire period that the FSRI Act has been in effect (*i.e.*, MY 2002-2005), Brazil has attempted in this proceeding to assert a breach of Articles 5(c) and 6.3(d) of the *SCM Agreement* on the basis of a slight (0.46 percent) up-tick in the U.S. share of the world market in MY 2005 over the average for MY 2002-2004.⁴⁸ The evidence on the record shows clearly that this increase in MY 2005 is part of the ordinary fluctuations in U.S. share of world supply⁴⁹ and is directly attributable to such factors as a sudden shift in acreage from soybeans in certain regions of the United States due to concerns about an outbreak of Asian soybean rust at

⁴⁷ U.S. First Written Submission, paras. 203-331 and Annex I; U.S. Rebuttal Submission, paras. 215-404 and Annex I; U.S. Answers to Parts A-C of First Set of Panel Questions, paras. 27-44; U.S. Oral Statement, paras. 50-85 and Statement of Dr. Joseph W. Glauber; U.S. Answers to Parts D-E of First Set of Panel Questions, paras. 14-42; U.S. Comments on Brazil’s “Oral” Presentation, paras. 34-91 and Annex I, and U.S. Answers to Second Set of Panel Questions, paras. 1-4, and 62-170.

⁴⁸ Brazil First Written Submission, paras. 222 and 224. This is the figure if one looks at U.S. share of world production plus beginning stocks. If one looks at U.S. share of world production, there was a similarly small increase (of 1.53 percent) over the average for MY 2002-2004.

⁴⁹ See U.S. First Written Submission, paras 332-343.

the end of MY 2004.⁵⁰ Thus, Brazil’s claim fails – at the outset – because Brazil cannot establish any causal connection between the challenged measures and the slight increase in U.S. world market share in MY 2005 (*i.e.*, it cannot prove the first of the two elements under Article 6.3(d), that “the effect” of the U.S. marketing loan and counter-cyclical payment programs “is an increase in the world market share” of the United States “as compared to the average share it had during the previous period of three years.”)

30. But Brazil’s claim also fails on a second basis – namely, Brazil’s failure to establish that “this increase” – *i.e.*, the “increase in the world market share of the subsidizing Member . . . as compared to the average share it had during the previous period of three years” – “follows a consistent trend over a period when subsidies have been granted.” This safeguard precludes complaining parties from establishing a breach under precisely the kind of factual circumstances before this Panel – where an increase in one year is clearly part of the normal fluctuation of world market share and attributable to any number of factors other than subsidies. As the United States showed in its first written submission and again in its rebuttal submission,⁵¹ the slight increase in U.S. market share above the previous three-year average has *not* followed a “consistent trend over a period when subsidies have been granted.” To the contrary, over the entire period that the FSRI Act of 2002 has been in effect there were only *one* year in which this happened – MY 2005.⁵²

31. To try to escape this key flaw in its claim, Brazil urges the Panel to adopt an end-point to end-point comparison using, as the starting point, MY 1998, a year before the entry into force of the FSRI Act of 2002 and one in which counter-cyclical payments were not even in existence. The reasons for Brazil approach are patently obvious – MY 1998 was a disastrous year for U.S. production, in which, as a result of severe drought U.S. abandonment rates skyrocketed and harvested area fell more than 2,000,000 acres compared to the previous year. U.S. production that marketing year was the lowest in almost a decade, by more than 1,500,000 bales, and lower than any marketing year *since* by more than 3,000,000 bales. By contrast, growers in the rest of the world, unaffected by the drought, increased harvested area about 100,000 acres. As a result, U.S. share of the world market was at an extremely low point in MY 1998. By selecting this

⁵⁰ See U.S. Comments on Brazil’s “Oral” Presentation, paras. 70-72.

⁵¹ The United States notes in this regard that Brazil devotes much effort in its answers to Questions 76-77 to attempting to characterize the U.S. interpretation of Article 6.3(d) as a “new” interpretation not previously presented. This is inexplicable given that in the U.S. first written submission, the United States clearly examined whether the U.S. world market share was higher than the average share of the previous 3-year period for each year in the periods MY 1996-2006, MY 1980-2006, and 1960-1996. This is the exact same examination conducted by the United States in its rebuttal submission. Indeed, Brazil appears to be confusing two separate issues – (a) the question of normal fluctuations in market share, which relates to the question of causation and whether in any particular year it is the challenged measures that are “causing” an increase over the previous three-year average and (b) the question of a “consistent trend” under the second element of Article 6.3(d).

⁵² This is true if one looks at world production. If one looks at world production plus beginning stocks, U.S. share of world supply would have been higher than the previous three-year average also in MY 2002.

year as the starting point of its “representative period,”⁵³ and drawing a line from this to the U.S. share of production in MY 2005 – one which would *inevitably* slant upwards – Brazil asserts that it has met its burden of showing that “this increase follows a consistent trend over a period when subsidies have been granted” under Article 6.3(d) of the *SCM Agreement*. Brazil is wrong. As the United States explains in its comments regarding Question 76, Brazil’s argument is premised on a fundamentally flawed interpretation of Article 6.3(d) of the *SCM Agreement*. That interpretation would – if adopted – effectively write out of Article 6.3(d) of the *SCM Agreement* both the reference to “this” increase and to a “consistent” trend. As Brazil fails to establish either of the two elements required under Article 6.3(d), it fails to make any *prima facie* of breach of that provision.

D. NEITHER THE MARKETING LOAN AND COUNTER-CYCLICAL PAYMENT PROGRAMS – NOR ANY PAYMENTS THEREUNDER – ARE CAUSING A “THREAT” SIGNIFICANT PRICE SUPPRESSION UNDER ARTICLES 5(C) AND 6.3(C) OF THE *SCM AGREEMENT*

32. There are two fundamental flaws in Brazil’s claims of “threat of” significant price suppression under Articles 5(c) and 6.3(c) of the *SCM Agreement*. The first is that Brazil’s claim is premised upon a legally incorrect interpretation of “threat of” significant price suppression. The second is that Brazil has not established as a factual matter that there is a “threat of” significant price suppression as a result of either the marketing loan and counter-cyclical payments programs or any payments under the programs. Brazil’s answers to the Panel’s questions regarding “threat” focus mostly on the first issue.

33. In its response to Questions 86-88, Brazil urges the Panel to replace the term “threat” in footnote 13 of the *SCM Agreement* with “significant likelihood,” a standard that Brazil admits is “not found in the *SCM Agreement* or any other WTO Agreement.”⁵⁴ Indeed, the only basis that Brazil has ever asserted for grafting a “significant likelihood” standard that drafters did *not* agree upon into footnote 13 is that “the precedent interpreting the terms ‘threat’ and ‘threaten’ suggests that the appropriate standard of threat in Part III [of the *SCM Agreement*] is one in which there is a significant likelihood, based on the nature of subsidies and particular conditions of competition, that serious prejudice will occur in the future.”⁵⁵ As the United States pointed out in its rebuttal submission, however, even leaving aside that there is no basis to attempt to interpret a treaty in accordance with “precedent” rather than “in accordance with customary rules of interpretation of public international law,”⁵⁶ Brazil cannot even identify any “precedent” that “suggests” that the appropriate standard for “threat” of serious prejudice is “a significant likelihood.”⁵⁷

⁵³ Brazil First Written Submission, para. 227.

⁵⁴ Brazil Answers to Second Set of Panel Questions, para. 182.

⁵⁵ Brazil First Submission, para. 253.

⁵⁶ DSU Article 3.2.

⁵⁷ U.S. Rebuttal Submission, para. 413.

34. Brazil’s proposed “significant likelihood” standard injects an entirely new term into the text that (a) is not used by the drafters either in Article 5(c) of the *SCM Agreement* or elsewhere to define “threat,” (b) ignores entirely a critical aspect of the ordinary meaning of the “threat,” (proximity in time) and (c) itself requires interpretation (e.g., what is a “significant” likelihood of serious prejudice). Brazil has provided no basis whatsoever for writing “significant likelihood” into footnote 13 of the *SCM Agreement*. And, indeed, to do so would contravene the express provisions of Article 3.2 of the DSU, which provides that “[the dispute settlement system of the WTO] serves . . . to clarify the *existing provisions of those agreements in accordance with customary rules of interpretation of public international law.*”

35. Brazil has also failed to establish an empirical basis for a finding of “threat” of serious prejudice. To the contrary, Brazil is asking the Panel to find that there is such a “threat” even though the evidence shows:

- an expected decline in U.S. planted acreage of more than 20 percent in MY 2007;⁵⁸
- an expected decline of 11 percent in U.S. production⁵⁹ in MY 2006 from year-before levels that is expected to continue on into MY 2007⁶⁰
- an expected decline in U.S. *share* of world production in MY 2007;⁶¹
- a 31 percent decline in U.S. exports going into the end of MY 2006 (compared to MY 2005 levels);⁶²
- that U.S. producers are likely to cover their variable, or operating, costs as well as a large share of their total costs in MY 2007 (even looking at the inflated “total costs” that Brazil has attempted to use repeatedly in this proceeding).⁶³
- that marketing loan payments are likely to be small (at most 2 cents/lb) in MY

⁵⁸ See U.S. Answers to Second Set of Panel Questions, paras. 1-4 (discussing NASS Prospective Plantings Report (March 30, 2007) (Exhibit US-140)).

⁵⁹ Indeed, just last month, USDA lowered expected production levels for MY 2007 even further. According to NASS, the MY 2007 U.S. upland cotton crop is now forecast at 20.8 million bales – down from the 21.3 million bales forecast in December 2006 – and approximately 11 percent below MY 2005 levels. NASS March 2007 Cotton Ginnings Report (Exhibit US-168).

⁶⁰ U.S. Export Sales Weekly Export Performance Indicator for Week Ending 4.12.2007, available at <http://www.fas.usda.gov/esrquery/esrpi.aspx> (Exhibit US-167).

⁶¹ Cotton This Month, ICAC, p. 4 (February 1, 2007) (Exhibit US-107).

⁶² U.S. Export Sales Weekly Export Performance Indicator for Week Ending 4.12.2007, available at <http://www.fas.usda.gov/esrquery/esrpi.aspx> (Exhibit US-167).

⁶³ U.S. Rebuttal Submission, paras. 422-425.

2007 and counter-cyclical payments – which are paid regardless of what is planted – are likely to remain at effectively “fixed” levels;⁶⁴ and

- the FSRI Act of 2002 is scheduled to expire in October of 2007 meaning that there will be no further payments thereunder as of MY 2008.

There is no basis for a finding of “threat” of serious prejudice under these circumstances.

E. THE UNITED STATES IS PROVIDING GSM 102 GUARANTEES IN RESPECT OF EXPORTS OF RICE AND UNSCHEDULED PRODUCTS CONSISTENTLY WITH ARTICLES 10.1 AND 8 OF THE AGREEMENT ON AGRICULTURE AND 3.1 AND 3.2 OF THE SCM AGREEMENT

36. In its responses to the Panel's questions – including Questions 92, 95, 100 – Brazil continues to urge the Panel to ignore the provisions of the *SCM Agreement* expressly setting out the conditions under which export credit guarantees may be found to be export subsidies and to make a finding that the provision of GSM 102 guarantees is prohibited simply because the fees under that program are allegedly lower than those charged by Ex-Im Bank for its Letter of Credit Insurance for Banks (“LCI”) and Medium-Term Export Credit Insurance (“MTI”) products. There is no support in the text or in logic for such a conclusion.

37. As the United States has explained, the drafters expressly set out in item (j) of the Illustrative List the conditions under which export credit guarantees may be found to be export subsidies. Brazil has not shown – and cannot show – that GSM 102 guarantees are provided “at premium rates which are inadequate to cover the long-term operating costs and losses of the” program. The data show that – to the contrary – for cohorts 1992-2002, examined by the original panel, the negative subsidy net of reestimates (*i.e.*, profit) is now \$926,331,216. For all cohorts 1992-2006, the negative subsidy net of reestimates (*i.e.*, profit) is \$403,714,701.⁶⁵ These are the figures under the U.S. government's credit reform accounting, which Brazil championed in the original proceeding as:

an ideal basis on which to determine whether the CCC's export credit loan guarantee programs are offered at premium rates that are inadequate to cover the long-term operating costs and losses of the programs, within the meaning of item (j) of the Illustrative List of Export Subsidies. It functions as a more sophisticated alternative to constructed cost formulas, and thoroughly accounts for all of the premium and operating cost and loss elements required by item (j). Moreover, it has the virtue of serving as the actual, real-world calculation used by the U.S. Congress, the President of the United States, and federal agencies like the CCC to

⁶⁴ See U.S. Answers to Second Set of Panel Questions, paras. 196-199 (showing that both FAPRI and CBO project at most a 2 cents/lb marketing loan payment for MY 2007.

⁶⁵ See U.S. Answers to Second Set of Panel Questions, paras. 277-278.

“measure more accurately the costs of Federal credit programs.”⁶⁶

38. Brazil has no basis for its arguments now – including in response to Question 114 – that the Panel should disregard this actual data and should use instead, Brazil constructed cost formula. The “the actual, real-world calculation used by the U.S. Congress, the President of the United States, and federal agencies like the CCC to ‘measure more accurately the costs of Federal credit programs’”⁶⁷ confirms that export credit guarantees under the GSM 102 program are being provided at premiums that are *well* above those that would be required simply to “cover” long-term operating costs and losses. Under the text of the *SCM Agreement*, the analysis begins and ends there. There is no “separate” standard under Articles 1.1 and 3.1(a) for when export credit guarantees constitute an “export subsidy.”

39. But even if item (j) did not exist, asserting that Ex-Im Bank charges higher fees for export credit guarantees than CCC does under the GSM 102 program would not establish any breach of Articles 1.1 and 3.1(a) of the *SCM Agreement*. As Article 14(c) of the *SCM Agreement* makes clear,⁶⁸ a loan guarantee provides a “benefit” recognized under Article 1.1 of the *SCM Agreement* only where it affects the underlying transaction – i.e., where it results in there being a “difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee.” This makes perfect sense. Export credit guarantees have no value in and of themselves; they simply modify and relate to the underlying loan transaction. It is only when they cause the underlying loan to be more attractive than loans otherwise available on the market that there is a possibility of trade distortion (*i.e.*, making a particular purchase of U.S. goods more attractive than it would have been absent the guarantee). The fee charged for a guarantee is passed through by the U.S. exporter to the foreign purchaser and becomes part of the overall cost of the financing. And it is only through the comparison of the total cost of loans guaranteed by GSM 102 guarantees and comparable commercial loans not guaranteed by GSM 102 guarantees that one can assess whether the GSM 102 guarantee actually rendered particular transactions more attractive than they otherwise would have been.

40. Brazil has not even attempted to make the kind of particularized showing contemplated under Article 14(c) of the *SCM Agreement*; it has not shown that the overall cost, including fees, of each of the loans guaranteed by the government is less than overall cost of a comparable commercial loan that could be obtained without a government guarantee. Instead, Brazil relies on sweeping and erroneous assertions that obligors on loans guaranteed under the GSM-102 program can *never* obtain any other financing of any kind and that the United States could *never* provide an export credit guarantee without also providing an export subsidy. These arguments

⁶⁶ Statement of Brazil - First (Original) Panel Meeting, para. 129 (22 July 2003).

⁶⁷ Statement of Brazil - First (Original) Panel Meeting, para. 129 (22 July 2003).

⁶⁸ Because it interprets and applies the definition of “benefit” set out in Article 1.1, Article 14 has been relied upon by the Appellate Body as important contextual guidance in interpreting “benefit.” *Canada – Aircraft (AB)*, para. 155.

simply do not square with the evidence submitted by the United States showing that such obligors are in fact able to obtain financing even without GSM 102 guarantees and on terms better than those available *with* GSM 102 guarantees. The declining level of use of the GSM 102 program in recent years is even further evidence of this.

41. Brazil's attempts to declare GSM 102 guarantees export subsidies merely on a comparison to fees charged by Ex-Im Bank are contrary to the text and logic of Articles 1.1(a), 14(c), and item (j) of the *SCM Agreement*. As the United States has explained, Brazil has not established that the LCI and MTI products are even comparable to the GSM 102 guarantees provided by CCC.⁶⁹ But, regardless of this, the reasoning underlying Brazil's comparison of these products is unavailing.

42. Brazil is effectively asking the Panel to assume that the LCI and MTI products are themselves provided at "below market" rates even though Brazil has conducted no actual comparison vis-a-vis any other comparable product available on the market. Following from this assumption, Brazil would have the Panel accept that, if the CCC charges lower fees than Ex-Im Bank, the fees for the GSM 102 guarantees must also be "below market." Brazil's approach is based on unfounded factual assumptions and on logic that is not found anywhere in the *SCM Agreement*. Member did *not* agree that export credit guarantees could be found to be export subsidies simply if one government entity charges fees that are different or lower than another government entity. Brazil's efforts to establish a breach of Articles 1.1(a) and 3.1(a) of the *SCM Agreement* on that basis are unavailing.

II. SPECIFIC COMMENTS REGARDING BRAZIL'S ANSWERS

A. Scope of this Proceeding

Questions to both parties

44. *The European Communities argues in respect of the preliminary objection raised by the United States regarding the claims of Brazil relating to export credit guarantees for pig meat and poultry meat under the GSM 102 programme that "the important issue is the nexus or the degree of interrelatedness or interdependence between different elements of the measure." (Oral Statement of the European Communities, para. 6) The European Communities submits in this regard that:*

"the Panel should examine the original measure at issue and the 'measures taken to comply,' and, with particular reference to the 'elements of the measure' that the United States argues are outside

⁶⁹ Brazil First Written Submission, para. 381

the Panel's terms of reference, enquire into the extent to which these are interrelated or interdependent with measures or 'elements of measures' that the United States accepts are within the Panel's terms of reference." (Oral Statement of the European Communities, para. 11)

Do the parties agree with the approach suggested by the European Communities and with the considerations in paragraph 13 of the Oral Statement of the European Communities?

43. The United States respectfully refers the Panel to its general comments above regarding Brazil's claims in respect of exports of pig meat and poultry meat as well as to its own response to this question.⁷⁰

45. Could the parties comment on the observations made by the European Communities in paras. 15-24 of its Oral Statement on the issue of whether the marketing loan and counter-cyclical payment programmes are within the scope of the Panel's proceeding?

44. The United States respectfully refers the Panel to its general comments above regarding Brazil's claims in respect of the marketing loan and counter-cyclical payment programs as well as to its own response to this question.⁷¹ The United States also submits one additional brief observation regarding Brazil's answer to this question.

45. The United States disagrees with Brazil's assertion that a claim about a measure "as such" is "typically understood to involve an examination of a general rule or norm in the abstract."⁷² An "as such" claim relates to whether the application of a measure in *all* present and future circumstances results in a breach of a covered agreement. This is not an inquiry "in the abstract" but the exact opposite, an inquiry across *all* of the possible factual circumstances that have and are expected to arise. Indeed, the Appellate Body underscored exactly this aspect of "as such" claims in *United States – Sunset Reviews on OCTG from Argentina*, where it explained that:

By definition, an "as such" claim challenges laws, regulations, or other instruments of a Member that have general and prospective application, asserting that a Member's conduct – not only in a particular instance that has occurred, but in future situations as well – will necessarily be inconsistent with that

⁷⁰ See U.S. Answers to Second Set of Panel Questions, paras. 1-16.

⁷¹ See U.S. Answers to Second Set of Panel Questions, paras. 17-41.

⁷² Brazil Answers to Second Set of Questions, para. 10.

Member's WTO obligations.⁷³

The Appellate Body explained that “as such” claims were to be considered to be “serious challenges” because “[i]n essence, complaining parties bringing ‘as such’ challenges seek to prevent Members *ex ante* from engaging in certain conduct.”⁷⁴

46. Despite this clarification from the Appellate Body about the caution to be exercised with “as such” challenges – and Brazil’s own acknowledgment, in response to this question, that a finding regarding the *effects* of a subsidy under Articles 5 and 6 of the *SCM Agreement* requires an examination of market conditions and the operation of the alleged subsidy within those conditions – Brazil would have the Panel believe that the original panel made a serious prejudice finding against the statutory and regulatory provisions authorizing Step 2, marketing loan, and counter-cyclical payment *programs* without so much as addressing the market conditions likely to prevail in the future. Rather, Brazil urges the Panel to ignore Brazil’s own express explanation to the original panel that the MY 1999-2002 period was “*both the period of time covering the measures challenged by Brazil* as well as the period of investigation to examine present serious prejudice caused by the U.S. subsidies under Articles 5(c) and 6.3 of the *SCM Agreement*” and its arguments in this proceeding that the MY 1999-2002 period presented an unusually “dynamic” situation for world market prices and U.S. exports.⁷⁵ Instead, Brazil would now have the Panel believe that the original panel simply used MY 1999-2002 as a reference period for the entire period of effectiveness of the FSRI Act of 2002. The facts simply do not support Brazil’s argument.

46. *In its Oral Statement, the European Communities characterizes Brazil's and the United States' respective approaches as the "measure model" and the "element of the measure model" (Oral Statement of the European Communities, para. 7). Please discuss whether you agree with this characterization and whether, in your view, the application of a measure alleged to be a subsidy to different agricultural products relates to a "measure" (or elements thereof) or if, rather it relates to a "claim". Would it be permissible for a compliance panel to examine a "claim" that relates to subsidies (granted as part of measures taken to comply) provided to agricultural products to which the "initial measure" did not apply?*

47. The United States respectfully refers the Panel to its general comments above regarding Brazil’s claims in respect of exports of pig meat and poultry meat, its comments regarding Brazil’s answer to Question 44 above, as well as to its own response to this question.⁷⁶

⁷³ *United States – Argentina OCTG Sunset Reviews (AB)*, paras. 172.

⁷⁴ *United States – Argentina OCTG Sunset Reviews (AB)*, paras. 172.

⁷⁵ Brazil Rebuttal Submission, para. 236.

⁷⁶ *See* U.S. Answers to Second Set of Panel Questions, paras. 1-16.

Questions to the United States

47. *The United States has raised a preliminary objection regarding Brazil's claims of (threat of) serious prejudice in respect of the marketing loan and counter-cyclical payment programmes. Is the Panel's understanding correct that, apart from this preliminary objection regarding programmes, the United States also considers that the issue of whether payments made under the marketing loan and counter-cyclical payment programme after 21 September 2005 cause serious prejudice to the interests of Brazil is not properly within the scope of this proceeding?*
48. *How does the United States address the argument of Brazil that “[i]f the United States were to prevail on its view that subsequent mandatory and price-contingent marketing loan and CCP payments are not properly before this Panel, the grant of annual recurring subsidies becomes ‘a moving target that escape from [the WTO subsidy] disciplines’”? (Closing Statement of Brazil, para. 4)*
49. *Could the United States comment on the argument of the European Communities that the text of Article 21.5 of the DSU does not limit the temporal scope of that provision in the manner suggested by the United States? (para. 29 of the Oral Statement of the European Communities)*

Question to Brazil

50. *Does Brazil maintain its claims with respect to the three unscheduled products (lyocell, lysine, wood products) identified by the United States as falling outside the scope of the Agreement on Agriculture? (see paragraph 83 of the United States' Rebuttal)*

48. In its response, Brazil appears to acknowledge that lyocell, lysine, and wood products fall outside the scope of the *Agreement on Agriculture*. By definition, therefore, the provision of GSM 102 export credit guarantees in respect of lyocell, lysine, and wood products cannot circumvent U.S. agricultural export subsidy commitments under that agreement.⁷⁷ In its request for establishment of a panel, Brazil presented claims under Articles 3.1 and 3.2 of the SCM Agreement “as a result and to the extent of [the alleged] violation of Article 10.1 (and, as a consequence, Article 8) of the *Agreement on Agriculture*.”⁷⁸ As there can be no “violation of Article 10.1 (and, as a consequence, Article 8) of the *Agreement on Agriculture*,”⁷⁹ there can be no claim under the *SCM Agreement* with respect to the GSM 102 export credit guarantees in

⁷⁷ U.S. Rebuttal Submission, paras. 81-83

⁷⁸ Brazil Request for Panel Establishment, para. 28.

⁷⁹ Brazil Request for Panel Establishment, para. 28.

respect of lyocell, lysine, and wood products under the express terms of Brazil's request for panel establishment. Where a claim is not set out in the request for panel establishment – as here – it is not part of the matter referred to the panel and falls outside the scope of a panel proceeding.

B. CLAIMS OF BRAZIL REGARDING PRESENT SERIOUS PREJUDICE

1. Significant price suppression - Article 6.3(c) of the SCM Agreement

Questions to both parties

51. *The parties disagree on whether or not the marketing loan and counter-cyclical payments have more than minimal effects on production of upland cotton. Could each party explain how its approach to the analysis of the impact of these payments on production of upland cotton is supported by the provisions of Articles 5 and 6 of the SCM Agreement and by any other relevant WTO provisions?*

49. The United States notes that, although the Panel's question asks each party to "explain how its approach to the analysis of the impact of [marketing loan and counter-cyclical] payments on production of upland cotton is supported by the provisions of Articles 5 and 6 of the SCM Agreement and by any other relevant WTO provisions," Brazil does not appear to actually answer this question. Rather, Brazil devotes almost all of its response to explaining why even green box measures can be subject to challenge under the *SCM Agreement*. This is inexplicable because Brazil then asserts that (a) the marketing loan and counter-cyclical payment programs are properly viewed as so-called "amber box" measures and (b) in the very next question, concedes that the fact that measures are classified in the "amber box" does not mean that they cause adverse effects within the meaning of Articles 5 and 6 of the *SCM Agreement*. It is difficult to understand, therefore, what – if anything – Brazil's answer has to do with explaining whether Brazil's approach is consistent with Articles 5 and 6 of the *SCM Agreement*.

50. Instead, Brazil's discussion seems to be aimed at suggesting that U.S. marketing loan and counter-cyclical payments should be found in breach of Articles 5 and 6 of the *SCM Agreement* no matter how minimal the effects thereof. Any such suggestion would be flatly wrong under the terms of those provisions. Only "subsidies" the effect of which is "significant" price suppression are subject to discipline by virtue of Articles 5(c) and 6.3(c) of the *SCM Agreement*. Whether any measures – whether green, blue, amber, or something else – may be *challenged* does not change the fact that the complaining party bears the burden of *proving* through evidence and argument that the challenged measures are causing adverse effects within the meaning of Articles 5 and 6 of the *SCM Agreement* (in the present case, "significant" price suppression under Article 6.3(c)). Where – as here – a complaining party fails to do so, its claim cannot succeed.

52. *In its Third Party Submission New Zealand observes:*

“Marketing loan payments are amber box measures, the category in which are included the non-prohibited measures with the most trade distorting effect on production and trade.” (para. 5.19)

Do the parties consider that the fact that under the Agreement on Agriculture a subsidy is included in the ‘amber box’ is relevant to the analysis of the subsidy's consistency with Articles 5 and 6 of the SCM Agreement?

51. The United States respectfully refers the Panel to the U.S. comments regarding Brazil's response to Question 51 above.

Questions to the United States

53. *The United States argues that Brazil has not provided evidence of ‘actual production inducing’ effects of marketing loan and counter-cyclical payments and that Brazil ‘purports to demonstrate indirect production effects through its claim that the US planting, production, and exports are not responsive to prices.’ (Opening Statement of the United States at the meeting of the Panel with the parties, paras. 62 and 69, emphasis in original)*

(a) *Could the United States explain further the distinction between what it terms “actual production inducing effects” and “indirect production effects”? Could the United States also elaborate on how this distinction is legally relevant in the context of Articles 5 and 6 of the SCM Agreement?*

(b) *What is the response of the United States to the argument that the fact that “U.S. upland cotton producers know that their overall revenue will always be protected by marketing loans and counter-cyclical payments ... plays a major role in their planting decisions”? (Rebuttal of Brazil, para. 185; see also Third Party Submission of New Zealand, paras 5.20-5.21)*

(c) *In its Opening Statement at the meeting of the Panel with the Parties, Brazil observed:*

“...we have demonstrated that these subsidies stabilized cotton producers' revenue despite wildly fluctuating market prices, thereby insulating and numbing acreage response to market price signals. These subsidies also

cover the huge long-term gaps between market returns and total costs of production. Both effects are closely interrelated.” (para.55)

Is the United States only arguing that Brazil has not empirically substantiated that these two “effects” have actually occurred or is it also the position of the United States that these effects are in any event legally irrelevant to an analysis of whether a subsidy causes significant price suppression within the meaning of Article 6.3 (c) of the SCM Agreement?

54. *Could the United States explain whether, and, if so, why, it is of the view that this Panel should not rely on the findings and analysis by the original Panel regarding the effects of marketing loan and counter-cyclical payments on production and exports? Please comment in particular on paras. 7.1291, 7.1295, 7.1302, 7.1349, 7.1353 of the Panel Report.*
55. *Can the United States confirm that the figures "\$868 million" and "\$838 million" Brazil cited in para. 40 of its Opening Statement are correct figures if one uses the "Brazil's methodology" and the "Cotton-to-Cotton methodology"? (Please note that the Panel is not asking whether the US agrees with these methodologies.)*
56. *The United States has cited new empirical research on the production effects of counter-cyclical payments. How does the United States address Brazil's criticism that none of this research has dealt specifically with the effects of countercyclical payments under the FSRI Act of 2002 on upland cotton? (Rebuttal Submission of Brazil, para. 120)*
57. *The United States has offered the Lin and Dismukes (Exhibit US-34) and Westcott (US-35) studies as examples of new empirical research on the production effects of counter-cyclical payments.*
 - (a) *Is it not more accurate to characterize the Lin and Dismukes study as a simulation of the possible effect of countercyclical payments on production rather than a study on the actual impact of the payments since it does not statistically estimate the effect of the actual payments (which began only in 2002) on crop production? (Please refer to pages 9-12 of the paper which describe the data, covering the period 1991-2001, used for the study).*
 - (b) *How does the United States deal with Brazil's characterization of the Westcott study as offering no new empirical evidence, and instead, being a qualitative discussion, much like that presented to the original panel*

(see para 128 of Brazil's rebuttal)?

58. *The United States stated that the key consideration in assessing a farmer's decision to grow upland cotton is whether the farmer has been covering his variable costs of production. In this connection, it presented upland cotton costs and returns estimates for marketing years 1999-2005 (Exhibit US-47). Brazil has disputed the absence of certain items – land, labour and capital recovery costs - in the US calculations of variable costs. In response, the United States has referred to the Commodity Costs and Returns Estimation Handbook (Exhibit US-88) prepared by a Task Force of the American Agricultural Economics Association as the basis for leaving out these items in its calculations. However, the Task Force which authored the Handbook does not use the categories "fixed" or "variable" costs and in fact recommends that the microeconomic concepts of fixed and variable costs not be used in preparing and reporting cost and return estimates. Page 2-67 of the Handbook states:*

The Task Force therefore recommends that costs should be categorized only as to whether they are associated with expendable factors or the services of capital assets. The division of costs into categories such as fixed and variable should generally be avoided in preparing CAR estimates. For the purpose of preparing CAR estimates for specific enterprises, the Task Force recommends that all the costs of all expendables be allocated to the generic group OPERATING COSTS and that all other costs be allocated to the group ALLOCATED OVERHEAD.

Would the United States clarify whether the categories "operating costs" and "allocated overhead" correspond to the economic concepts of fixed and variable costs? In particular, are "operating costs" variable costs or not? Would the United States please indicate whether, and if so, where, the Handbook makes these clarifications or distinctions.

59. *In discussing the impact of long-term costs of production (and hence long-term profitability) of upland cotton production on farmers' decisions to exit cotton farming, the United States argues that income from other crops and off-farm income must be into account. Why does the United States consider these issues relevant given the original Panel's decision that "off farm income" is not a legally relevant consideration. (Panel Report, para. 7.1354, footnote 1470) Please respond to Brazil's arguments on this matter in paragraphs 249-253 of its Rebuttal Submission.*
60. *In its Rebuttal Submission, the United States argues that Prof. Sumner's*

description of the model that appeared in a recent CATO publication is not “appropriate” for use in a WTO dispute involving claims of serious prejudice. Professor Sumner has since introduced “more empirical and institutional detail” to the model used in this dispute. These changes are described in paragraphs 111-117 of Brazil's Opening Statement. Does the United States view these changes as being sufficient to make the model appropriate for use in a WTO dispute involving claims of serious prejudice? If not, what modifications does the United States think should have been made to the model?

61. *With respect to marketing year 2006, the United States has provided some data on upland cotton exports (Exhibit US-113), planted and harvested area and cotton production (Exhibit US-114), as well as a copy of the National Cotton Council's survey of planting intentions (Exhibit US-115). The data, all of which have been collected through the first half of marketing year 2006, are variously qualified as “estimates” or “projections” or “projected.”*
- (a) *Please clarify, as completely as possible, what these various terms mean as they apply to US upland cotton exports, acreage and production.*
- (b) *Would the United States be able to provide the Panel with some information, based on the average of the past six marketing years or so, of how final marketing year data on these variables, would differ from preliminary estimates, projections and the like, taken at the end of February of the relevant marketing year?*
- (c) *Finally, would the United States be able to update that part of Exhibit US-83 dealing with futures prices so as to provide the panel with as complete as possible average January to March 2007 New York futures prices for upland cotton?*

Questions to Brazil

62. *How does Brazil rebut the argument of the United States that the fact that marketing loan and counter-cyclical payment programmes provide income support when prices are low is not the key question before this Panel and that while, like any other payments to producers, marketing loan and counter-cyclical payments could affect production, Brazil has not provided any evidence of actual production-inducing effects? (Rebuttal Submission of the United States, paras. 222, 287-291; Opening Statement of the United States at the meeting of the Panel with the parties, paras. 62-75; Comments of the United States on Brazil's 'Oral' Presentation in the meeting with the Panel, paras. 42-57)*

52. Brazil's response to the first part of this question highlights that fact that Brazil is attempting to have the Panel find income support to agricultural producers to effectively be a prohibited measure under the *SCM Agreement*.

53. Indeed, Brazil asserts as “one of the fundamental facts supporting Brazil's adverse effects claims”⁸⁰ the mere *fact* that marketing loan and counter-cyclical payment programs provide income support to U.S. producers at times of low prices. Similarly, Brazil argues that it is evidence of price suppression under Articles 5(c) and 6.3(c) of the *SCM Agreement* that U.S. farmers “know” that if prices fall below certain levels, they may receive payments under the marketing loan and counter-cyclical payment programs. As the United States explained in its response to Question 53(b), however, *any* eligible recipient of income support “knows” that he or she will receive some income protection due to those payments. That is the very nature and intent of income support programs – to ensure that producers receive some income that they would not otherwise get on the market.

54. In fact, U.S. farmers are even more secure in their “knowledge” that they will receive such payments where payments are fixed, as in the case of direct payments (*i.e.*, as compared to payments under the marketing loan and counter-cyclical payment program, which depend on U.S. and world market prices that are not within the control of individual farmers and cannot even be known until many months after the decision is made whether or not to plant cotton). Yet, as the original panel recognized in the case of direct payments,⁸¹ the fact that farmers have such “knowledge” does not necessarily result in any “adverse effects” within the meaning of Articles 5 and 6 of the *SCM Agreement*.

55. As the United States has noted before, most economists agree that direct payments, like marketing loan payments, counter-cyclical payments, payments supporting elderly or low-income recipients or, for that matter, *any* type of payment to a producer of agricultural products will have some effect on risk and wealth and that this may, in turn, have some effect on production. The question under Articles 5(c) and 6.3(c) is whether Brazil has shown that – taking into account the particular structure and design of the programs and the way they operate under the market conditions prevailing at present – payments under the programs are having actual effects on production that are so substantial that they are resulting in “present” *significant* price suppression. It is significant price suppression that is precluded under the SCM

⁸⁰ Brazil Answers to Second Set of Questions, para. 44.

⁸¹ Brazil's assertions about the alleged “key role” that direct payments allegedly play in “allowing many upland cotton farmers to achieve a healthy ‘profit’ from growing upland cotton” – even though direct payments are not at issue in the present proceeding – is further evidence of Brazil's efforts to render income support a prohibited measure under the *SCM Agreement*. Brazil Answers to Second Set of Questions, para. 56. According to Brazil, “such profits play an important role in maintaining upland cotton production over the longer term by increasing the ‘wealth’ of producers.” Brazil Answers to Second Set of Questions, para. 56. What Brazil asserts is true of any payment to any agricultural producer; any such payment would “increas[e] the ‘wealth’ of producers.” This does not mean that all payments to producers are causing “significant” price suppression.

Agreement, not any *possible* effect on production or any *actual* effect on production that does not ultimately result in significant price suppression in the market identified by the complaining party.

56. Brazil's response to the second part of the Panel's question – asking Brazil to respond the U.S. observation about the lack of an empirical basis for Brazil's claims of "present" serious prejudice – confirms that Brazil has not established such actual "present" effects. Thus, for example, Brazil cites as "evidence" findings made by the original panel and the Appellate body about the collective effects of a different set of measures (Step 2, marketing loan and market loss assistance or counter-cyclical payments) in a different period of time (MY 1999-2002) and under different market conditions.⁸² These findings are not directly relevant here. Moreover, as the United States explained in its response to Question 54,⁸³ the factual observations that the original panel made regarding marketing loan and counter-cyclical payments in reaching its conclusion about the collective effects of the Step 2, marketing loan and counter-cyclical payments made in MY 1999-2002 do not support a finding that marketing loan and counter-cyclical payments are causing "significant" price suppression at present under the existing market conditions.

57. Brazil then asserts that a "strong link" "has been recognized" by various entities between the programs and payments challenged by Brazil in this proceeding and upland cotton acreage, production, exports, and prices.⁸⁴ However, *not a single one of the sources* Brazil cites actually looks to the collective effects of the marketing loan and counter-cyclical payments on world market prices, let alone looks at whether these effects amount to significant price suppression under the market conditions existing in the "present" (*i.e.*, MY 2006). Indeed, Brazil even goes as far as to cite as "evidence" a U.N. Food and Agricultural Organization ("FAO") report that observes that "all of the recent studies unambiguously demonstrate that *the removal of domestic subsidies in industrialized countries* reduces cotton production in and exports from these countries."⁸⁵ There is no basis whatsoever to find that U.S. marketing loan and counter-cyclical payments are causing "present" significant price suppression within the meaning of Articles 5(c) and 6.3(c) of the *SCM Agreement* simply on the basis that they are "domestic subsidies in [an] industrialized countr[y]."

58. Moreover, contrary to Brazil's assertions, the FAO report does *not* suggest that there is a "strong link" between the marketing loan and counter-cyclical payments and upland cotton

⁸² As Brazil confirmed in the first (resumed) meeting with the original Panel, "[t]he four-year period in which these subsidies [the "subsidies provided for the production, export and use of U.S. upland cotton during the period MY 1999-2002"] were provided is both the period of time covering the measures challenged by Brazil as well as the period of investigation to examine present serious prejudice caused by the U.S. subsidies under Articles 5(c) and 6.3 of the SCM Agreement." Brazil's 7 October 2003 Second Statement at First Panel Meeting, para. 3 (emphasis added)

⁸³ U.S. Answers to Second Set of Panel Questions, paras. 101-106.

⁸⁴ Brazil Answers to Second Set of Questions, para. 45.

⁸⁵ Brazil Answers to Second Set of Questions, para. 45.

acreage, production, exports or prices.⁸⁶ The FAO report simply reviews a number of different studies examining the removal of various domestic support measures and/or tariffs from the cotton sector in a number of countries (some even looking at removal of such measures world-wide). As Brazil has acknowledged, the original panel reviewed similar studies during the course of its analysis and “recognized that many of the parameters including magnitude, and time period of the subsidies, elasticities, measures, and selection of baselines did not address exactly the time period or legal issues before the original panel.”⁸⁷ Accordingly, the *only* conclusion that the original panel considered appropriate to draw from these widely divergent, inapposite studies – according to Brazil – was that “subsidies bestowed by Member governments have the *potential* to distort production and trade.”⁸⁸ This does not equate to the recognition of any “strong link.”

59. Brazil also points to statements by a U.S. trade association made before enactment of the 2002 farm bill purporting to show that U.S. farmers would be “bankrupt” without marketing loan and counter-cyclical payments. Again, not one of these statements pertain to marketing loan or counter-cyclical payments. Rather, they were made about emergency relief provided under the FAIR Act of 1996 in the period MY 1999-2001. These statements – quoted out of context – about an entirely different set of measures (including disaster payments), offers no insight regarding the role of marketing loan and counter-cyclical payments in production decisions or about U.S. farmers’ costs and revenues today. Certainly it does nothing to detract from the actual data regarding “present” costs and revenue, which, as discussed in the prior U.S. submissions, flatly contradict Brazil’s claims that U.S. upland cotton farmers would be bankrupt without the marketing loan and counter-cyclical payment programs.

60. What is conspicuous in its almost complete absence from Brazil’s listing of the evidentiary basis for its claims is evidence of any present production-inducing effects of the marketing loan and counter-cyclical payments under the market conditions prevailing at present and without the Step 2 program in place. Indeed, the *only* argument that Brazil makes about the effects of marketing loan and counter-cyclical payments under the current market conditions is that, according to a U.S. “market expert,” current U.S. stocks will allegedly “keep a heavy lid on the market” and, in term of prospective plantings, that “any total acreage number below 12.5 million acres will be bullish. The lower the intended plantings, the higher the price rally.”⁸⁹

⁸⁶ Brazil Answers to Second Set of Questions, para. 45.

⁸⁷ Brazil Rebuttal Submission, para. 309.

⁸⁸ Brazil Rebuttal Submission, para. 309. Indeed, the FAO itself concludes that any potential distortion may be minimal. The FAO estimates price effects of *only* 3.1 to 5 percent and it does so for “*complete elimination of domestic subsidies as notified to the WTO and tariffs;*” in other words, *every domestic support and every tariff for every country in the world that notifies either to the WTO*. Poonyth, Daneswar, et al., “The Impact of Domestic and Trade Policies on the World Cotton Market,” FAO Commodity and Trade Policy Research Working Paper No. 8, April 2004, p. *i* (Exhibit US-55). Any possible effect of U.S. domestic supports – let payments under only *two* of the U.S. programs – would necessarily be substantially less. This is hardly evidence of a “strong link.”

⁸⁹ Brazil Answers to Second Set of Questions, para. 51.

61. Brazil's assertion that this is "evidence" of significant price suppression is misleading. The question under Articles 5(c) and 6.3(c) is whether U.S. marketing loan and counter-cyclical payments significantly suppress world market prices for upland cotton. Whether or not increased U.S. stocks may have some effects on prices does not answer that question. Any effects on prices could only be attributed to U.S. marketing loan and counter-cyclical payments to the extent that Brazil proves that it was marketing loan and counter-cyclical payments that *caused* all of the production that is placed in inventory. Brazil clearly has not done so.⁹⁰

62. Absent specific evidence regarding the effects that marketing loan and counter-cyclical payments are having at present under the prevailing market conditions, Brazil has no basis for its claims of "present" serious prejudice under Articles 5(c) and 6.3(c).

63. *Could Brazil explain whether or not it considers that whether marketing loan and counter-cyclical payments increase acreage is not relevant to the inquiry of whether these payments cause significant price suppression within the meaning of Article 6.3 (c) of the SCM Agreement? (para. 56 of the Opening Statement of Brazil) Could Brazil comment on the points made by the United States in footnote 72 of the Comments of the United States on Brazil's "Oral" Presentation in the meeting with the Panel?*

63. The United States notes that the bulk of Brazil's answer to this question addresses arguments that have never been made by the United States. The United States has never suggested that "Article 6.3 of the *SCM Agreement* . . . compel[s] a complaining Member to produce evidence that the challenged subsidies result in a steady *increase* in production or acreage."⁹¹ Therefore, it is inexplicable why Brazil devotes nearly four pages of argument in an attempt to rebut such an assertion.

64. Rather, as the Panel's question itself reflects in its reference to footnote 72 of the Comments of the United States on Brazil's "Oral" Presentation in the meeting with the Panel, the United States has taken issue with Brazil's inexplicable arguments in its unsolicited third written submission – BRA-659 – that the Panel should disregard a number of the studies submitted by

⁹⁰ The market analysis submitted by Brazil actually *confirms* that – contrary to Brazil's assertions – U.S. production and exports/stocks are not primarily responsible for the upland cotton market trends that are currently being observed. Specifically, the actual planting intentions figures for MY 2007 were far lower than those predicted by the "market expert" cited by Brazil – the report forecasted U.S. upland plantings to be only 11.86 million acres. NASS Prospective Plantings Report (March 30, 2007) (Exhibit US-140). This is 20.7 percent lower than MY2006 acreage and over 600,000 acres below the point at which the "market expert" predicted there would be a "bullish" impact on prices. Yet, both the May and December futures contracts for upland cotton, as quoted by the New York Board of Trade, *declined*, on average, since the report was issued. N.Y. Futures After Issuance of Planting Intentions Report (Exhibit US-169). This is hardly the "bullish" response predicted and confirms that other factors – such as China's upland cotton trade balance – are very much responsible for the world market price phenomenon that experts are trying to understand. As discussed in response to Question 74 below, Brazil has never properly accounted for these other factors in its assessment of "present" serious prejudice.

⁹¹ Brazil Answers to Second Set of Questions, para. 59.

the United States because they do “not examine whether CCPs are decoupled from production. Rather, [they] examine whether CCPs increase acreage.”⁹²

65. The United States appreciates Brazil's acknowledgment now, in response to this question, that its focus on “coupling” in the language cited by the United States was misplaced: “the notion of “coupled” and “decoupled” support in the Agreement on Agriculture . . . is not relevant for the assessment of the effects of subsidies under Articles 5 and 6 of the SCM Agreement.”⁹³ Rather, as Brazil now concedes the salient question is whether marketing loan and counter-cyclical payments cause such substantial shifts in planted acreage that oversupply, export, and ultimately “significant” price suppression within the meaning of Articles 5(c) and 6.3(c) of the *SCM Agreement* result.⁹⁴ As discussed in the prior U.S. submissions⁹⁵ and above in the general comments of the United States regarding Brazil's claims under Articles 5(c) and 6.3(d) of the *SCM Agreement*, the evidence before the Panel does *not* support Brazil's arguments that the marketing loan and counter-cyclical payments are causing any such significantly suppressed world market prices.

64. *Given that Brazil has criticized the new empirical research cited by the United States because it does not deal specifically with the effects of countercyclical payments on upland cotton production, why does Brazil consider that the McIntosh, Shogren & Dohlam study (Rebuttal Submission of Brazil, para. 140) is particularly relevant to this case? Could Brazil comment on the arguments of the United States in paragraphs 248-249 of the Rebuttal Submission of the United States?*

66. Brazil fails to establish why the McIntosh, Shogren & Dohlam study – a study that does not address upland cotton specifically and that is premised on highly restrictive assumptions about the operation of the counter-cyclical program – is “more applicable to the assessment that the compliance Panel is tasked with”⁹⁶ than the many studies submitted by the United States.

67. Indeed, it is important to note that – because the McIntosh, Shogren & Dohlman study is not limited to upland cotton production – its results are presumably supposed to be valid even for

⁹² Supplementary Statement of Daniel Sumner, para. 21.

⁹³ Brazil Answers to Second Set of Questions, para. 65. Brazil's attempts to attribute the focus on “coupling” to the United States in its response is, however, patently unfounded, as the U.S. discussion in footnote 72 (reflected above) clearly shows.

⁹⁴ Brazil Answers to Second Set of Questions, para. 66.

⁹⁵ U.S. First Written Submission, paras. 203-331 and Annex I; U.S. Rebuttal Submission, paras. 215-404 and Annex I; U.S. Answers to Parts A-C of First Set of Panel Questions, paras. 27-44; U.S. Oral Statement, paras. 50-85 and Statement of Dr. Joseph W. Glauber; U.S. Answers to Parts D-E of First Set of Panel Questions, paras. 14-42; U.S. Comments on Brazil's “Oral” Presentation, paras. 34-91 and Annex I, and U.S. Answers to Second Set of Panel Questions, paras. 1-4, and 62-170.

⁹⁶ Brazil Answers to Second Set of Questions, para. 67.

predicting effects on wheat, corn, and soybean acreage. However, it comes to *directly* inconsistent conclusions about the effects of counter-cyclical payments on wheat, corn, and soybean acreage than the studies submitted by the United States (for example, the Lin & Dismukes study finding that “[t]he effect of CCPs on producers’ planting decisions . . . appears to be *very negligible* – an increase in the acreage of major field crops of less than 1%”)⁹⁷ Although Brazil has argued that the Panel should ignore those other studies because they are not specific to upland cotton, Brazil has never explained why the McIntosh, Shogren & Dohlman study should be viewed as reliable when it comes to such different conclusions about the effects of counter-cyclical payments even with respect to the other crops. Indeed, the divergence in the results for wheat, corn, and soybean acreage simply confirm what the United States has argued and the authors of the McIntosh, Shogren & Dohlman study themselves acknowledge⁹⁸ – that this study overstates any effects of counter-cyclical payments on acreage.

68. The authors themselves identify some of the reasons why that particular study overstates any effects of counter-cyclical payments on acreage. Namely:

Our design did not address two features of the 2002 Act which could affect the interpretation of our results. First, there are no adjustments made in our bonuses for the fact that direct and counter-cyclical payments are made only on a percentage (85 percent) of base acres. If these adjustments were incorporated, the lump sum bonuses would have been lower, implying our results could overstate the effects of CCPs. Second, we excluded the marketing loan program to focus on the basic CCP structure—target price, market price, and direct rate. Adding the marketing loan program into our design would temper the basic effects of CCPs by providing an additional price support mechanism.⁹⁹

69. There are other reasons as well that have to do with the kind of laboratory experiments upon which the McIntosh, Shogren & Dohlman study is premised. The use of a laboratory experiment may allow the researchers to focus on a particular set of problems or issues but necessarily abstracts away from other highly relevant factors that also affect a producer’s

⁹⁷ Lin, William and Dismukes, Robert. “Supply Response Under Risk: Implications for Counter-cyclical Payments’ Production Impacts,” *Review of Agricultural Economics—Volume 29, Number 1—Pages 64-86*, forthcoming, p. 83 (Exhibit US-85) (emphasis added).

⁹⁸ McIntosh, Christopher R, Jason F. Shogren and Erik Dohlman, “Supply Response to Counter-Cyclical Payments and Base Updating under Uncertainty: An Experimental Study,” forthcoming paper in the *American Journal of Agricultural Economics*, November 2006, page 18 (Exhibit BRA-565). The United States notes that this citation is in error since the article did not appear in the November 2006 issue of the *American Journal of Agricultural Economics*.

⁹⁹ McIntosh, Christopher R, Jason F. Shogren and Erik Dohlman, “Supply Response to Counter-Cyclical Payments and Base Updating under Uncertainty: An Experimental Study,” forthcoming paper in the *American Journal of Agricultural Economics*, November 2006, page 18 (Exhibit BRA-565). The United States notes that this citation is in error since the article did not appear in the November 2006 issue of the *American Journal of Agricultural Economics*.

planting decision. Thus, for example, Brazil cites the authors of the McIntosh, Shogren & Dohlman study as noting that “farmers have other risk management tools at their disposal; large and less risk-averse farms tend to dominate production of program crops; and other programs such as marketing loan provisions already offer price protection.”¹⁰⁰ The McIntosh, Shogren & Dohlman study excludes these factors in assessing the effects of counter-cyclical payments. Yet, as Paul Westcott et. al. explained,¹⁰¹ it is precisely these kinds of factors that mitigate and temper any *actual* effects of counter-cyclical payments.¹⁰² To ignore these factors is to improperly attribute to counter-cyclical payments effects that they do not *actually* have in the real world but only have in some artificial vacuum created for purposes of a laboratory experiment. It says little about whether counter-cyclical payments are *actually* having the kind of production effects alleged by Brazil and whether those effects are *actually* lead to the kind of price suppressive effects with which Article 6.3(c) is concerned.

70. What Brazil presents – in short – is a highly abstract study with limited conclusions.¹⁰³ The laboratory experiment upon which the study is based does not reflect the economic

¹⁰⁰ See Brazil Answers to Second Set of Questions, para. 68, n. 63 (citing McIntosh, Christopher R., Jason F. Shogren and Erik Dohlman, “Supply Response to Counter-Cyclical Payments and Base Acre Updating under Uncertainty: An Experimental Study,” Forthcoming paper in the American Journal of Agricultural Economics, November 2006, p. 16-17 (See Exhibit BRA-565)).

¹⁰¹ The original panel found an earlier version of Westcott’s analysis to be persuasive as to the effects of counter-cyclical payments.

¹⁰² Paul A. Westcott, “Counter-Cyclical Payments Under the 2002 Farm Act: Production Effects Likely to be Limited” at 203-205 (Exhibit US-35). Westcott notes in this regard that: (a) where prices are expected to be above maximum threshold – counter-cyclical payments behave just like the fixed direct payments; (b) “cross-commodity effect[s] suggest[] that CCPs may provide a general reduction in revenue risks rather than a crop-specific effect. Net returns among alternative crops would remain the primary consideration underlying production choices;” (c) “while a number of studies indicate that farmers are risk averse (Chavas and Holt, 1990, 1996, for example), other risk reduction instruments already exist to manage risks. Thus, with revenue risk reduction now provided by CCPs as part of farm programs, farmers may adjust their use of these other farm and nonfarm risk management strategies;” and (d) “a large portion of output in the U.S. agricultural sector is produced by a small share of large producers. . . . Evidence that risk aversion decreases as income rises (Chavas and Holt, 1990, 1996) suggests that risk aversion may also tend to decline as the size of farms increases. Thus, with larger farms that account for most production being less averse to facing risk, this lowers potential production effects of CCPs due to risk reduction. And while smaller farms may be more risk averse in their farm enterprise, off-farm income may reduce the overall level of household income risk.” Paul A. Westcott, “Counter-Cyclical Payments Under the 2002 Farm Act: Production Effects Likely to be Limited” at 203-205 (Exhibit US-35). On the basis of these and other factors, Westcott concludes that “there are several mitigating factors which suggest that overall production effects of CCPs through revenue risk reduction are likely to be limited.” Paul A. Westcott, “Counter-Cyclical Payments Under the 2002 Farm Act: Production Effects Likely to be Limited” at 205 (Exhibit US-35). The other studies submitted by the United States examining the empirical evidence of production effects – for example, including the Lin & Dismukes study finding that “[t]he effect of CCPs on producers’ planting decisions . . . appears to be *very negligible* – an increase in the acreage of major field crops of less than 1% . . .” – confirm that the effects of the counter-cyclical payments are, in fact, very limited. Lin, William and Dismukes, Robert. “Supply Response Under Risk: Implications for Counter- cyclical Payments’ Production Impacts,” *Review of Agricultural Economics–Volume 29, Number 1–Pages 64-86*, forthcoming, p. 83 (Exhibit US-85) (emphasis added).

¹⁰³ Brazil Answers to Second Set of Questions, para. 68.

conditions of actual upland cotton producers.¹⁰⁴ Rather, the experiment “mimicked” certain stylized scenarios to attempt to isolate and measure the impact risk aversion and uncertainty might have on production decisions.¹⁰⁵ In doing so, however, the authors removed from consideration some of the most critical factors that affect the degree to which farmers are, in fact, risk averse, such as the size of the enterprise and the availability of other price hedging mechanisms. Moreover, they exclude important factors other than risk that affect a farmer's planting decisions. When *all* factors are taken into account – as reflected in the empirical data used by some of the other studies submitted by the United States – a much more realistic picture emerges of the effects of counter-cyclical payments.

71. Brazil also claims that the McIntosh, Shogren & Dohlman study is more relevant because it is not confined to the geographic regions of other studies.¹⁰⁶ That is a curious argument given that Brazil at once asserts that geographical factors may have some effect on the effects of counter-cyclical payments and asserts that a study that takes *none* of these factors into account is somehow the most reliable measure of the effects of counter-cyclical payments. In any event, Brazil's criticism that the Lin & Dismukes and Goodwin & Mishra studies on corn, soybeans, and wheat are less relevant to upland cotton because supply elasticities for these crops are much smaller than for upland cotton is only valid if one ascribes to the inflated supply elasticity used by Brazil in its Sumner II (CATO) model. For the reasons explained in the prior U.S. submissions, it is not appropriate to do so.¹⁰⁷

72. Finally, the United States notes that Brazil misstates the U.S. arguments. The United States has not criticized the field of behavioral or experimental economics, nor has the United States suggested that the McIntosh, Shogren & Dohlman is invalid merely because it is based on controlled experiments, as Brazil claims.¹⁰⁸ Rather, the United States has identified the numerous factors that limit the utility of the McIntosh, Shogren & Dohlman study in assessing the question at hand, including those expressly acknowledged by its authors. Moreover, the United States has noted the irony in Brazil's criticisms leveled at the studies submitted by the United States (*i.e.*, that they are not unique to upland cotton production), when Brazil itself submits studies that do not even examine the behavior of actual farmers but, rather, the responses of University of Wisconsin economics students to some highly stylized scenarios. To claim that this highly abstract experimental study “analyzes more closely the effects of counter-cyclical

¹⁰⁴ Brazil Answers to Second Set of Questions, para. 69.

¹⁰⁵ McIntosh, Christopher R., Jason F. Shogren and Erik Dohlman, “Supply Response to Counter-Cyclical Payments and Base Acre Updating under Uncertainty: An Experimental Study,” Forthcoming paper in the *American Journal of Agricultural Economics*, November 2006, p. 5) (Exhibit Bra-565).

¹⁰⁶ Brazil Answers to Second Set of Questions, para. 69.

¹⁰⁷ See *e.g.*, U.S. First Written Submission, paras. 319-328 and Annex I; U.S. Rebuttal Submission, paras. 349-386 and Annex I; U.S. Oral Statement, paras. 76-81 and Statement of Dr. Joseph W. Glauber; U.S. Comments on Answers to Parts D-E of First Set of Panel Questions, paras. 30-42; and U.S. Comments on Brazil's “Oral” Presentation, paras. 79-91.

¹⁰⁸ Brazil Answers to Second Set of Questions, para. 71.

payments on the production decisions of U.S. upland cotton farmers than results of empirical studies”¹⁰⁹ – as Brazil does – is simply not supported by a review of the study and its conclusions.

65. *The United States has cited new empirical research on the production effects of counter-cyclical payments. Could Brazil explain why the fact that these studies do not deal specifically with upland cotton should preclude the Panel from considering the studies as being highly probative?*

73. Brazil's answer to this question fundamentally contradicts its answer to Panel question 64. Brazil asserts that the studies submitted by the United States are not probative “due to their failure to address the specific effect of upland cotton counter-cyclical subsidies on upland cotton production.”¹¹⁰ Yet, as Brazil admits in Question 64 there are no studies that “address the specific effect of upland cotton counter-cyclical subsidies on upland cotton production.”¹¹¹ and in fact that studies upon which it relies itself – including the McIntosh, Shogren & Dohlman study – do not even do so. Brazil's complaint on this basis is, thus, patently absurd.

74. Equally unavailing are the four bases that Brazil asserts for why the effects of counter-cyclical payments made to a holder of upland cotton base acreage that produces upland cotton should be understood to be fundamentally different from those observed by Lin & Dismukes for counter-cyclical payments made in respect of corn, wheat, and soybeans and Goodwin & Mishra for marketing loss assistance payments in respect of the same crops. For example, Brazil does not explain what its assertions about “maximum per-acre counter-cyclical payments” have to do with effects on production. In fact, if it were true – as Brazil alleges – that the costs of production for upland cotton are higher than for other crops, one would expect rational farmers to produce other crops while still collecting the allegedly very high maximum upland cotton counter-cyclical payment. Thus, Brazil's reasoning actually supports exactly the opposite conclusion than the one it asserts.

75. Brazil's assertions about the “frequency of payment” similarly lack merit. Differences in what Brazil calls the “fill rate” did not preclude Brazil's preferred study – the McIntosh, Shogren & Dohlman study – from presenting one single assessment across all counter-cyclical payments. This supports the conclusion that any alleged differences in the “frequency of payment” do not preclude the Lin & Dismukes and Goodwin & Mishra from being highly probative of the likely effects of counter-cyclical payments made in respect of upland cotton base acres.

76. Brazil's third asserted basis – its allegation that “one would expect low supply elasticities

¹⁰⁹ Brazil Answers to Second Set of Questions, para. 73.

¹¹⁰ Brazil Answers to Second Set of Questions, 75.

¹¹¹ Brazil Answers to Second Set of Questions, 75.

in these regions for these crops”¹¹² – is similarly without merit. As noted in response to Question 64, this appears to be premised on Brazil's own assertions of grossly inflated supply elasticities for upland cotton.

77. Finally, as noted above, there is no basis for Brazil's attempts to invoke certain statements by the NCC carefully selected to give the impression that U.S. upland cotton farmers would simply be “bankrupt” without counter-cyclical payments. As Brazil admits, these statements were not even made with respect to counter-cyclical payments under the FSRI Act of 2002 but rather were made in February 2001 – before the FSRI Act of 2002 even came into effect – about certain emergency relief that had been provided under the FAIR Act of 1996 including production flexibility contract payments, marketing loss assistance payments, and disaster payments. These statements offer no insight regarding the role of counter-cyclical payments in production decisions or about U.S. farmers' costs and revenues today. And they certainly do nothing to detract from the actual data regarding “present” costs and revenue, which flatly contradict Brazil's claims that U.S. upland cotton farmers would be bankrupt without counter-cyclical payments.

78. In sum, Brazil has offered no valid reason why the Panel should not consider the studies submitted by the United States to be highly probative on the question of the effects of the counter-cyclical payments on acreage and production decisions. The United States submits that these studies continue to provide important insight into the effects of those payments and confirm the U.S. arguments that these effects are not the “significant” production and price effects that Brazil has alleged.

66. ***Can Brazil explain the differences between the figures for the amount of counter-cyclical payments allocated to upland cotton provided by Brazil at the meeting of the Panel with the parties (Opening Statement of Brazil, para. 40 and Exhibit Bra 625) and the figures in Table 5 of Brazil's Rebuttal Submission?***
67. ***Please confirm whether or not the Panel's understanding is correct: “Table 6” in Brazil's First Written Submission was produced using the so-called “Brazil's method” using USDA data. “Table 5” in Brazil's Rebuttal Submission was produced using the so-called “cotton-to-cotton” methodology using USDA data. The figures cited in para. 40 of Brazil's opening statement (i.e. “\$868 million and \$838 million) are produced with the “Brazil's method” as well as the “cotton-to-cotton” methodology, using the data provided by the United States in exhibit US-64.***
68. ***Please comment on the following statement by the US:***

¹¹² Brazil Answers to Second Set of Questions, para. 80.

“The United States understands that Brazil intends the counter-cyclical payment figures shown in ‘Table 5’ of Brazil’s rebuttal submission to supersede the counter-cyclical payment figures shown in ‘Table 6’ of its first written submission.” (US response to question 4 at para. 15)

69. *How does Brazil address the argument of the United States that “the only evidence that Brazil has submitted purporting to examine the price effects of marketing loan and counter-cyclical payments specifically are the results of the modelling exercise that it has conducted for purposes of this proceeding”? (Opening Statement of the United States, para. 76)*

79. In the cited portion of the U.S. oral presentation, the United States observed that:

regarding the *degree* of any possible effects on world market prices, the United States notes that the *only* evidence that Brazil has submitted purporting to examine the price effects of marketing loan and counter-cyclical payments specifically are the results of the modeling exercise that it has conducted for purposes of this proceeding.¹¹³

80. Brazil accuses the United States of “ignor[ing] the hundreds of exhibit and the circumstantial evidence presented by Brazil in the original proceeding and in this compliance proceeding,”¹¹⁴ and then expounds for 10 pages about the “abundant and diverse evidence” it has allegedly presented.¹¹⁵ However, not a single piece of the allegedly “abundant and diverse evidence” does what the United States noted – examines the degree of any possible effects on world market prices of the marketing loan and counter-cyclical payment programs. The United States therefore understands Brazil’s response to confirm the U.S. observation.

81. As to Brazil’s assertion that its allegedly “abundant and diverse evidence” nonetheless supports a finding that “the effect” of marketing loan and counter-cyclical payments is “present” significant price suppression, Brazil is wrong. The United States has addressed each of Brazil’s arguments in its prior submissions,¹¹⁶ in the general U.S. comment above regarding Brazil’s

¹¹³ U.S. Oral Statement, para. 76.

¹¹⁴ Brazil Answers to Second Set of Questions, para. 90.

¹¹⁵ Brazil Answers to Second Set of Questions, para. 101.

¹¹⁶ U.S. First Written Submission, paras. 203-331 and Annex I; U.S. Rebuttal Submission, paras. 215-404 and Annex I; U.S. Answers to Parts A-C of First Set of Panel Questions, paras. 27-44; U.S. Oral Statement, paras. 50-85 and Statement of Dr. Joseph W. Glauber; U.S. Answers to Parts D-E of First Set of Panel Questions, paras. 14-42; U.S. Comments on Brazil’s “Oral” Presentation, paras. 34-91 and Annex I, and U.S. Answers to Second Set of Panel Questions, paras. 1-4, and 62-170.

claims under Articles 5(c) and 6.3(c), and in the U.S. comments regarding Brazil's responses to Questions 62-65 and 70. As shown therein, none of the "evidence" asserted by Brazil withstands scrutiny.

70. How does Brazil respond to the United States' rebuttal that Brazil has not even established a temporal correlation between payment of subsidies and significantly suppressed prices during the life of the FSRI, that is from marketing year 2002 to 2005? More specifically, please address the United States' claim of the stability of US plantings, US share of world production, US share of world exports and the world price of cotton during this period.

82. The United States notes that Brazil chooses not to respond to the Panel's question. The Panel asks Brazil to "respond to the United States' rebuttal that Brazil has not even established a temporal correlation between payment of subsidies and *significantly suppressed prices during the life of the FSRI, that is from marketing year 2002 to 2005.*" Instead of responding, however, Brazil attempts to sidestep the issue by attributing to the United States – inexplicably – the "assertion" that "there were not 'coincidences' between (a) *increased U.S. production and exports* and (b) large U.S. marketing loan and counter-cyclical subsidies" and then proceeding to attempt to rebut that alleged "assertion."¹¹⁷ The United States has never suggested that this is the appropriate analysis, let alone made the kind of "assertions" that Brazil attempts to attribute to the United States. Nor did the original panel conclude that an increase in absolute levels of production and exports would equate to a "temporal coincidence" between allegedly *significantly suppressed world market prices* and payments under the marketing loan and counter-cyclical payment program.

83. Rather, the original panel considered a number of factors *every single one* of which the United States examined in its first written submission and its rebuttal submission.¹¹⁸ As the United States showed therein, none of the factors considered by the panel in the original proceeding in reaching its conclusion of a "discernible temporal coincidence" between U.S. subsidies and significant price suppression support such a finding with respect to the marketing loan and counter-cyclical payments now. Brazil has never rebutted the U.S. arguments in this regard; and does not do so now even despite the direct request by the Panel to do so. This confirms that Brazil has not – and cannot – prove any "discernible temporal coincidence" between significantly suppressed world market prices and marketing loan and counter-cyclical payments. Indeed, as discussed below, Brazil has not even proven the factual predicates therefor, including significantly suppressed prices.

84. Rather than offering any proof of "discernible temporal coincidence" between significantly suppressed world market prices and marketing loan and counter-cyclical payments, Brazil relies on reasoning that is entirely untenable. Consider, for example, Brazil assertion that

¹¹⁷ Brazil Answers to Second Set of Questions, para. 108.

¹¹⁸ U.S. First Written Submission, paras. 277-291; U.S. Rebuttal Submission. paras. 314-320.

the increase in the absolute level of U.S. production and exports alone over the life of the FSRI Act of 2002 should be understood “in isolation” to “suggest a relationship” between the marketing loan and counter-cyclical subsidies and allegedly suppressed world market prices.¹¹⁹ As evidenced by the fact that U.S. share of world production and exports has remained relatively stable over the course of the entire FSRI Act, however, it is a fact that there is *precisely* the same “temporal coincidence” between increased foreign production and exports and the U.S. marketing loan and counter-cyclical payments. Does this – “in isolation” – support the same conclusion in respect of *foreign* production and exports? Should the U.S. marketing loan and counter-cyclical payments be understood to have *caused* the increase in the absolute level of *foreign* production and exports? Surely not. Surely any rational analysis would look more closely at how the marketing loan and counter-cyclical payments interact with the production decisions (i.e., the decision on what to plant).

85. When one looks at planted acreage, one finds that the *increase* of absolute levels of U.S. production is solely attributable to an increase in yields. In fact, in MY 2005, U.S. producers actually planted *fewer* acres than in either MY 2001 or MY 1999 (13.9 compared to 15.4 and 14.5 million acres, respectively), the years that Brazil has urged the Panel to look at as comparison years before the FSRI Act came into effect. Moreover, had the yields in MY 2005 been what they were in those earlier years, U.S. production in MY 2005 would have been far lower.¹²⁰ Thus, contrary to Brazil's assertions, the increased production in these years is not evidence of any causal link between the marketing loan and counter-cyclical payments and production. It is evidence of dramatic improvements in yields.

86. In an apparent effort to avoid this flaw in its argument, Brazil then argues that “but for” the U.S. marketing loan and counter-cyclical payments, U.S. planted acreage would have been lower over the life of the FSRI Act.¹²¹ As the United States has shown – examining the planting decisions made by U.S. farmers in MY 2006, MY 2005 and, in fact, every year under the FSRI Act of 2002 – the facts do not support Brazil's assertion.¹²² Thus, Brazil's answer only confirms that, notwithstanding its assertions, Brazil does not – and, in fact, cannot – “reinforce the original panel's finding, at paragraph 7.1351 of its report, of a discernable temporal coincidence of suppressed world market prices and the price-contingent U.S. subsidies.”¹²³

87. Nor does Brazil respond fully to the second of the Panel's questions. As the Panel's

¹¹⁹ Brazil Answers to Second Set of Questions, para. 109.

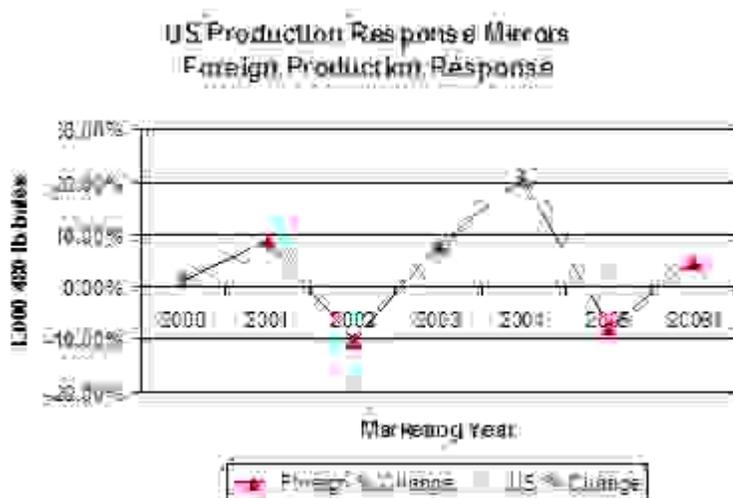
¹²⁰ If yields were at the levels that prevailed in MY 2001, U.S. production would have been almost 30 percent lower in MY 2005. If yields were at MY 1999 levels, U.S. production would have been almost 40 percent lower. See U.S. First Written Submission, paras. 279-282.

¹²¹ Brazil Answers to Second Set of Questions, para. 108.

¹²² See e.g., U.S. Comments on Brazil's “Oral” Presentation, paras. 58-78.

¹²³ Brazil First Written Submission, para. 152. The United States notes that, while Brazil asserts in its first written submission that it will isolate the effects of the marketing loan and counter-cyclical payment programs, it does not do in its assessment of “temporal coincidence.”

question reflects, the United States identified a key flaw in Brazil theory at the very start of this proceeding.¹²⁴ Namely, if, as Brazil alleges, U.S. producers were cut off from market signals, why does U.S. production response mirror foreign production response (see chart below)? Why does one not find U.S. share of world production and exports increasing over the life of the FSRI Act as U.S. producers allegedly ignore the same market signals received by their foreign counterparts?



88. Brazil has never been able to rebut this evidence; its only response has been to assert that the stable share of world production and exports is somehow itself evidence that U.S. producers are insulated from market signals. However, as the United States explained in its first written submission, in making this assertion, Brazil is improperly assuming its own conclusion – *i.e.*, “stable U.S. share of world production and export proves that U.S. support payments cause price suppression because without the price suppression caused by U.S. support payments U.S. share of world production and exports would not be stable.”¹²⁵ Brazil’s circular reasoning is not improved by its reassertion in Brazil’s response to this question.

89. In its response, Brazil also argues at length about the alleged “United States [*sic*] claims that the stability of U.S. acreage demonstrates the lack of any ‘temporal coincidence’ (and hence causation).”¹²⁶ Brazil’s arguments in this regard are baffling because the United States has not “claimed” any such thing. What the United States has noted is (a) the original panel’s analysis that “United States production of upland cotton increased from MY 1998 to MY 2001 and, while production dropped in MY 2002, there was still an overall increase in MY 2002 compared to

¹²⁴ U.S. First Written Submission, paras. 243-252.

¹²⁵ U.S. First Written Submission, para. 251.

¹²⁶ Brazil Answers to Second Set of Panel Questions, paras. 112-115.

MY 1998;¹²⁷ and (b) *Brazil’s* arguments that in its discussion of production and “temporal coincidence” in the panel report, “[t]he [original] Panel simply referred to “production” as shorthand for planting decisions by producers, which even in agricultural economics literature is not uncommon.”¹²⁸ According to Brazil’s argument, then, the original panel found an “overall increase” in the U.S. upland cotton planted acreage in MY 1999-2002 and considered this as one factor in its finding of a “discernible temporal coincidence”. The United States has shown that there is no similar “overall increase” in the U.S. upland cotton planted acreage over the life of the FSRI Act. To the contrary, planted acreage declined from MY 2002 levels in MY 2003 and MY 2004, picked up slightly in MY 2005 and more so in MY 2006 but is projected to fall dramatically in MY 2007 to levels lower than they have been in almost a decade.¹²⁹

90. There is similarly no merit to the other arguments made by Brazil regarding U.S. planted acreage.¹³⁰ Brazil continues to make arguments on the fundamentally flawed assumption that U.S. planted acreage should change year-to-year based on changes in the futures price for upland cotton alone. Thus, for example, Brazil even claims as “one of the most important ‘temporal coincidences’ in the record” – the fact that U.S. planted acreage increased slightly in MY 2005 even though futures prices for cotton in that year were lower than the year before.¹³¹ But Brazil’s own assertions about the proper analysis of planted acreage in another year – MY 2007 – demonstrate the fallacy in Brazil’s arguments about planted acreage shifts in MY 2005. If U.S. planted acreage must move in synch solely with upland cotton prices, why does Brazil argue that U.S. upland cotton acreage should be *decline* dramatically in MY 2007¹³² even though the expected harvest time price for upland cotton in this year (*i.e.*, the average January-March 2007

¹²⁷ *Upland Cotton (Panel)*, para. 7.1351.

¹²⁸ Brazil Appellee Submission, para. 686. Brazil argued that “ultimate production” is not an appropriate basis for assessing production *decisions* as “producers do not decide on production, but on plantings. Ultimate production is affected by weather and other factors affecting yields.” Brazil Appellee Submission, para. 706, n. 995. As a result, Brazil asserted that the original panel’s discussion of an “overall increase in production” was actually a discussion regarding planting, not actually production.

¹²⁹ See U.S. First Written Submission, para. 280 and U.S. Answers to Second Set of Panel Questions, paras. 1-4

¹³⁰ As the United States explained in its rebuttal submission, Brazil’s attempts to compare changes in U.S. *planted acreage*, changes in foreign *harvested* acreage, and *changes* in the futures prices is fundamentally flawed both because of its apples-to-oranges comparison and also because it seeks to explain changes in U.S. upland cotton acreage *solely* by reference to upland *cotton* futures, in disregard of the basic fact that acreage decisions are made in consideration of prices and other factors not only for cotton but for competing crops. U.S. Rebuttal Submission, paras. 305-306. In fact, what Brazil’s flawed analysis shows – when conducted on the same harvested-acreage basis for both the United States and the rest of the world – is that *neither* U.S. nor foreign harvested acreage moves closely in line with futures prices of cotton alone. U.S. Rebuttal Submission, para. 305-307. Nonetheless, even if the comparison were valid (and it is not), it would show that, where changes in U.S. and foreign area diverge, U.S. harvested acreage tends to react more *conservatively* than foreign acreage to increasing prices (as in MY 2003 and 2006). U.S. Rebuttal Submission, paras. 305-307. This would undermine – rather than support – Brazil’s assertions of alleged “subsidy-fueled overproduction.”

¹³¹ See U.S. Comments on Brazil’s “Oral” Presentation, para. 70.

¹³² Oral Statement of Brazil, para. 73.

New York futures price for the December contract) is 59 cents/lb, more than 6 cents/lb *higher* than for MY 2005 and almost the same level as in MY 2006. The reason why Brazil argues that there should be a decline is because the prices for *corn* – a competing crop – make that a more attractive option in MY 2007.¹³³ The same kind of considerations of competing crops, weather, pests and other such factors – not some narrow assessment of changes in the futures price for upland cotton price alone – explain the acreage shifts also in MY 2005 (and indeed in each of the other years that the FSRI Act has been in effect).¹³⁴

91. Finally, the United States notes that although the Panel asks Brazil specifically to respond to the U.S. arguments regarding world market prices, Brazil does not do so. Rather, Brazil simply asserts that prices over the life of the FSRI Act are below those that prevailed in MY 1980-1998.¹³⁵ As the United States explained in its first written submission, however, Brazil’s claim in this proceeding is of significant price *suppression*, not price *depression*. A *decline* in prices does not demonstrate price *suppression*.¹³⁶ The question is whether prices are being prevented from *rising* by something (in this case, the marketing loan and counter-cyclical payment programs). Brazil provides no empirical evidence showing such “suppression” as a result of marketing loan and counter-cyclical payments.

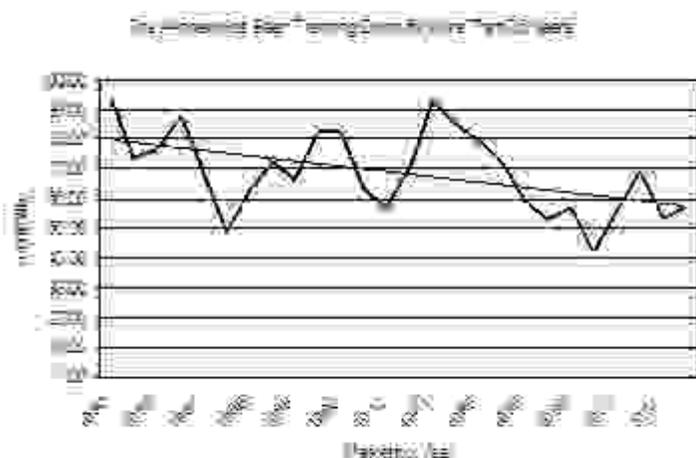
92. Rather, the fact that the A-Index has trended downwards for more than 25 years now – well before the FSRI Act came into effect – and the fact that the A-Index has gone *up* from the levels that prevailed *before* the FSRI Act came into effect as of MY 2002 would tend to suggest that, to the extent there is any price *suppression*, it is not “the effect” of the marketing loan and counter-cyclical payment programs.

¹³³ See Brazil Oral Statement of Brazil, para. 73 (arguing that “[i]f marketing loan and CCP subsidies did not exist, and if U.S. cotton farmers would have to react to market price signals, far more than 14 percent of cotton acreage predicted by the NCC [for MY 2007] would switch to substitute crops.”); see also U.S. Comments on Brazil’s “Oral” Presentation, paras. 1-4 (rebutting Brazil’s argument).

¹³⁴ See U.S. Comments on Brazil’s “Oral” Presentation, para. 70. For example, the data show a perfect correlation between a shift away from soybean acreage in MY 2005 due to concerns about an outbreak of Asian soybean rust in the Delta and Southeast regions of the United States and an increase in the competing crop – cotton – in the exact same areas.

¹³⁵ Brazil Answers to Second Set of Questions, para. 113.

¹³⁶ Interpreting “suppression” in accordance with its ordinary meaning of “[p]revent or inhibit (an action or phenomenon),” the panel in the original proceeding defined “price suppression” as “the situation where ‘prices’ – in terms of the ‘amount of money set for sale of upland cotton’ or the ‘value or worth’ of upland cotton – either are prevented or inhibited from rising (i.e. they do not increase when they otherwise would have) or they do actually increase, but the increase is less than it otherwise would have been.” *Upland Cotton (Panel)*, paras. 7.1276-7.1277. The Appellate Body agreed that this was an appropriate interpretation of “price suppression.” *Upland Cotton (AB)*, para. 424.



Source: USDA, Agriculture Marketing Service Reports¹³⁷

93. Brazil has never rebutted this evidence nor established that there is a “discernible temporal coincidence” of U.S. marketing loan and counter-cyclical payments and allegedly suppressed world market prices.

71. *In the original case, the Panel concluded that the analysis covering "the six-year period from 1997-2002 ... lends itself to an assessment of the medium- to longer-term examination of developments in the United States upland cotton industry" (see para. 7.1354 of the original panel report). Thus, total costs of production were the costs considered appropriate by the Panel. Would total costs of production continue to be relevant should the compliance Panel decide to use only marketing year 2005 as the reference period for analysis? Or would variable costs of upland cotton farming in marketing year 2005 now be the relevant information to consider?*

94. The United States offers a number of observations regarding Brazil's answer to this question. First, Brazil asserts that there have been no fundamental changes in the conditions of competition or any other relevant factors that would compel the compliance Panel to reject the findings of the original panel's causation analysis relating to “total cost of production.”¹³⁸ Brazil is incorrect.

95. As the United States explained as early as September 2003, the 1997 ERS/USDA survey data on cost of production used by both Brazil and the United States in the original panel

¹³⁷ Compiled Statistics – Prices (Exhibit US-25).

¹³⁸ Brazil Answers to Second Set of Questions, paras. 117 and 118.

proceeding likely overstated certain costs because of technological and other changes.¹³⁹ The U.S. arguments were borne out when ERS released new cost of production data based on a 2003 survey. As a result of changes in technology – widespread adoption of biotech cottonseed, and other improvements in production practices, such as boll weevil eradication programs – upland cotton yields have exhibited a structural increase and per unit input costs have fallen.¹⁴⁰ This dramatic shift in the cost and yield structure for upland cotton certainly represents a fundamental shift in the conditions of competition, contrary to Brazil's assertions. As the United States explained in earlier submissions, the data show clearly that upland cotton producers covered not only their operating (variable) costs but also a substantial portion of their total costs between 2002-2005.¹⁴¹

96. Second, Brazil continues to assert that total costs of production, including non-cash or economic costs, are determinative of a producer's planting decision, without offering any basis in the economic literature or even in fact to support that assertion. The United States has reviewed this issue thoroughly in its prior submissions and, rather than repeating this here, refers to the Panel to the earlier discussion.¹⁴² For the reasons explained by the United States, if the Panel were to examine effects on planting/production in a single year – MY 2005 – the relevant consideration is operating costs, not "total" costs.¹⁴³

97. Third, while Brazil is correct in its observation that a farmer has two different cost concerns – one a year-to-year planting decision and another long-term decisions about the economic viability of his farm – Brazil analysis of these decisions is flawed. As the United States has explained the "total costs" that Brazil uses is not an appropriate consideration with respect to either decision.¹⁴⁴ To the extent a producer has planting options for various crops, based on agronomic conditions, the first decision is an assessment of net returns per crop; that is, what is relative market revenue minus operating costs (net revenue per crop).¹⁴⁵ In addition, over time, a producer must also cover all cash costs, including such items as mortgage costs and equipment. The United States agrees with Brazil that "without generating sufficient funds to meet this second set of costs, there would be no facilities or equipment to grow upland cotton in the first place."¹⁴⁶ However, as the United States has shown, U.S. farmers assess the economic

¹³⁹ U.S. Further Submission in the original panel proceeding, paras. 46-54 (September 30, 2003). U.S. Further Rebuttal Submission in the original panel proceeding, para. 123-133 (November 18, 2003).

¹⁴⁰ U.S. First Written Submission, December 15, 2006, para. 302.

¹⁴¹ U.S. First Written Submission, December 15, 2006, para. 300.

¹⁴² For the most recent review, see U.S. Comments on Brazil's "Oral" Presentation, paras. 62-65.

¹⁴³ Any such analysis would also have to look at the other factors besides expected operating costs affect the planting decision – MY 2005 being a good example of other confounding factors. In that year, a major unanticipated factor was the emergence of soybean rust in key cotton producing states, which encouraged producers to switch from soybeans to cotton. U.S. Comments on Brazil's "Oral" Presentation, para. 70.

¹⁴⁴ See U.S. Answers to Second Set of Panel Questions, paras. 96-100, 113-116, 133-154.

¹⁴⁵ See e.g., U.S. Comments on Brazil's "Oral" Presentation, paras. 66-67.

¹⁴⁶ Brazil Answers to Second Set of Questions, para. , para. 121.

viability of a farm *based on the total costs and revenue for the farm*.¹⁴⁷ It is on the basis of those considerations – not some artificially segmented crop-by-crop “total cost” analysis – that the farmer makes decisions such as whether to declare bankruptcy.

98. It is a significant flaw in Brazil’s analysis, therefore, that Brazil disregards off-farm income and income from other crops, both of which are an important part of the total revenue of a farm. It is similarly incorrect for Brazil to attempt to include in its “total cost” analysis such factors as imputed opportunity costs that have been calculated by USDA to attribute some value to unpaid labor and owned land but that are not necessarily costs that must be paid off in order for farmers to avoid having to “close down [their] business[es].”¹⁴⁸ As a result of these flaws, the picture that emerges of the financial viability of U.S. farmers is completely and thoroughly distorted. It results in the attribution to marketing loan and counter-cyclical payment “effects” that they are not in fact having.

99. When one considers instead, the total cash costs that most farmers do in fact have to meet over the long term, the data show that U.S. farmers have in fact generated sufficient funds to cover their total cash costs over the long term. The cost data for the period 2000-2005 show that, instead of the cumulative \$663 *deficit* per acre erroneously asserted by Brazil, the cumulative returns over the same period were a *positive* return of \$161 per acre. Moreover, for MY 2000-2006, instead of the \$837 *deficit* per acre alleged by Brazil, the cumulative net returns were a positive \$133 per acre.¹⁴⁹

100. The FAPRI baseline projections from July 2006, which Brazil used in an earlier submission, confirm the same facts. Comparing gross market revenue for upland cotton per acre to variable expenses per acre shows that upland cotton revenue would more than cover variable expenses and would cover a large share of other cash expenses. For the period 2004/05 - 2010/11, cumulative net returns per acre were projected to be \$620.34.¹⁵⁰

101. It is important to remember that these results look *only* to total costs and revenue for upland cotton production. When whole-farm costs and revenue from all sources is taken into consideration an even more robust picture of economic viability would likely emerge.

72. *Brazil has argued that the adjustment in cotton stocks should not be included in the simulation of a large and permanent reduction in subsidies to cotton. Please respond to the following argument:*

If the simulation were a comparative static analysis in

¹⁴⁷ See e.g., U.S. Answers to Second Set of Panel Questions, paras. 133-154.

¹⁴⁸ *Upland Cotton (Panel)*, para. 7.1353.

¹⁴⁹ U.S. Comments on Brazil’s “Oral” Presentation, paras. 76-77.

¹⁵⁰ Brazil’s First Written Submission, para. 286. See also Exhibit Bra-479, page 6.

which a baseline is compared to a counterfactual outcome in some long-run state, modelling such adjustments would be unnecessary. But such adjustments should be taken into account given that the model is used to simulate the average impact on the world price of cotton (among other variables) on specific periods of time (MY 2002-05 or MY 2006-08) and not in the long run.

102. In its response to this question, Brazil continues to suggest incorrectly that stock responses are incorporated into the demand elasticities used in Brazil's new model. This is simply untrue.

103. Brazil also attempts to minimize the importance of stock adjustments to overall market price movements. However, stock-holding activity is an important component of any storable commodity market. Market participants hold stocks for a variety of reasons to accommodate a number of possible factors. The adjustment of stocks is an important determinant in overall price movement. The United States has shown that by ignoring the importance of stocks in a short-run analysis, Brazil's analysis overstates the price impacts.¹⁵¹

104. The United States agrees that stock adjustments are not necessary to an analysis of long-term demand and price adjustments. However, in a long-term analysis, the elasticities that are used must fully reflect long-term adjustments in supply and demand. Based on such elasticities documented by FAO, the United States demonstrated that – even using Brazil's own econometric model, which suffers from certain fundamental structural flaws that tend to overstate the results – any price impacts due to the removal of U.S. programs are only in the range of 1 to 1.5 percent, not the grossly exaggerated results that Brazil attempts to show.

73. *How does Brazil respond to the argument made by the United States in paragraph 79 of its Opening Statement that:*

“to the extent a counterfactual assessment is undertaken, it is only to assess what the price equilibrium would be at present if marketing loan and counter-cyclical payments had been lower, different or did not exist. Article 6.3(c) does not ask what prices will look like in the short-run adjustment period if the marketing loan and counter-cyclical payments are suddenly eliminated... Brazil's argument that it is necessary to look at the short-run effects of total elimination of the programs cannot be accurate as a textual matter.”

¹⁵¹ See e.g., U.S. Comments on Brazil's "Oral" Presentation, para. 86.

More specifically:

(a) *Why did Brazil not consider it appropriate to include simulations that involve reductions rather than elimination of the subsidy programmes?*

105. The United States offers two observations in respect of Brazil’s answer. First, Brazil’s response to this question appears to make little sense. Brazil asserts that it has not modeled reductions of the U.S. marketing loan and counter-cyclical payment programs because the United States has not made changes to reduce payments under those programs. However, the United States has also not *eliminated* the marketing loan and counter-cyclical payments. Under its own reasoning, Brazil would have no basis for purporting to model the total elimination of those payments either.

106. Second, the United States notes that Brazil reasserts its arguments about the appropriateness of assessing the “short-run” response of “shocking” the system with elimination of marketing loan and counter-cyclical payments. As the United States has explained, Brazil confuses the question under Articles 5(c) and 6.3(c) of the *SCM Agreement*. The question under those provisions is what the present effects of the challenged measures are (and whether these effects comprise “significant” price suppression). The question is not what the effects are of *eliminating* anything. To the extent a counterfactual analysis is conducted to attempt to tease this out, the question is simply where the equilibrium would have been *today* had the challenged measures not been in existence. The question is not what *will* happen in the *short run* if a Member were to eliminate the challenged measures today. Brazil’s citation of *Korea – Ships* confirms this precisely:

price suppression is the situation where prices have been restrained by something, and price depression is the situation where prices have been pushed down by something. So the question to be answered is whether the “something” is subsidization. Looking at a counterfactual situation, i.e., trying to determine *what prices would have been in the absence of the subsidy*, seems to us the most logical and straightforward way to answer this question.¹⁵²

107. Indeed, in other disputes, Brazil has confirmed that in assessing trade effects using a counterfactual analysis, “elasticity values should be taken from long-run estimates and not short run estimates.”¹⁵³ Brazil has provided no valid reason for why the analysis is different here.

(b) *If simulations of such scenarios are performed, would the current values of the elasticities chosen (particularly the supply elasticities) to simulate the elimination of marketing loan and counter-cyclical programmes continue to be appropriate? Please kindly provide an*

¹⁵² *Korea – Ships (Panel)*, para. 7.612.

¹⁵³ *U.S. – Continued Dumping and Subsidy Offset Act (22.6)*, para 3.101.

explanation for the chosen answer.

108. The United States is surprised by Brazil's assertion now that its inflated U.S. supply elasticity is actually appropriate even for assessing a partial reduction of payments under U.S. programs. Brazil itself has argued that different elasticities are necessary for reduction of payments versus "permanent" removal of payments and has attempted to have the Panel dismiss the FAPRI parameters on the basis that they are not applied to "permanent" removal of payments.¹⁵⁴ Now – however – the Panel is to believe that the inflated Sumner elasticities are nonetheless appropriate for use in every context. Brazil's assertions about these elasticities simply lack credibility. The United States has shown that the modeling parameters and assumptions that Brazil uses are grossly exaggerated.¹⁵⁵ This is true regardless of whether they put to an analysis of partial or full reduction of payments.

74. *Brazil's view is that the data that the Panel must consider for its claim of present serious prejudice should be that covering the latest marketing year for which complete information is available, MY 2005, and where credible, evidence after 31 July 2006. Since in MY 2005, payments under Step 2 continued to be made by the United States (payments which the original Panel found to have contributed to adverse effects) how shall the Panel ascertain that any adverse effects observed in marketing year 2005 are due solely to the two subsidy measures which are the subject of the present serious prejudice claim – marketing loan and counter-cyclical payments?*

109. The United States offers three observations about Brazil's answer to this question. First, Brazil's response to this question provides an interesting contrast to its response to Question 69 above. In that response, Brazil attempts to excuse its failure to provide empirical evidence regarding the effects of the marketing loan and counter-cyclical payment programs on the basis that "Brazil cannot unilaterally remove the U.S. subsidies to present direct evidence of what would actually happen to U.S. acreage, production, exports, and world prices without those subsidies. Only the United States can do so."¹⁵⁶ In its response to this question, however, Brazil argues that where the United States *has* removed a domestic support program, the Panel should

¹⁵⁴ Brazil's assertions about the FAPRI parameters are patently untrue. FAPRI has used their modeling system to analyze the removal of domestic subsidies under trade liberalization scenarios and the reduction of farm subsidies under various farm bill scenarios, including the "permanent" removal of payments. Indeed, in attempting to argue that elimination of the Step 2 program has had no effects on exports or prices, Brazil itself submitted and repeatedly cites to a FAPRI assessment of the effects of eliminating that program. See Brazil First Written Submission, para. 203 (addressing FAPRI, "Impacts of Commodity and Conservation Reserve Program Provisions in House and Senate Reconciliation Bills," FAPRI-UMC Report #15-05, December 2005(Exhibit Bra-484).)

¹⁵⁵ See e.g., U.S. First Written Submission, paras. 319-328 and Annex I; U.S. Rebuttal Submission, paras. 349-386 and Annex I; U.S. Oral Statement, paras. 76-81 and Statement of Dr. Joseph W. Glauber; U.S. Comments on Answers to Parts D-E of First Set of Panel Questions, paras. 30-42; and U.S. Comments on Brazil's "Oral" Presentation, paras. 79-91.

¹⁵⁶ Brazil Answers to Second Set of Questions, para. 91.

not rely primarily on the “direct evidence of what would actually happen to U.S. acreage, production, exports, and world prices without” payments under that program but rather on Brazil’s own “counterfactual” assertions about the effects of the removal of the Step 2 program (which are, in any event, heavily contradicted by the arguments presented by Brazil itself in the original panel proceeding and undermined by the empirical evidence).¹⁵⁷ In effect, Brazil suggests that – regardless of what the facts actually are and regardless of whether payments are being made under the challenged programs or not – the Panel must rely on whatever Brazil alleges about the effects of the payments. There is no basis for such a suggestion.

110. Second, the facts relating to the period after the removal of the Step 2 program – which Brazil attempts to have the Panel ignore – show U.S. plantings declining and U.S. exports declining dramatically even as the cost structure of U.S. upland cotton farms improves due to such factors as the use of genetically modified cottonseed. Brazil has not established that, despite these facts, U.S. marketing loan and counter-cyclical payments are somehow “significantly” suppressing world market prices. The decline in exports and the decline in predicted plantings are occurring even though both the marketing loan program and the counter-cyclical payment program remain in place and even though – according to Brazil – these programs are allegedly “designed” to provide consistently high payments to U.S. farmers. These facts are not consistent with the theories that Brazil has put forward purporting to establish the alleged “numbing” of U.S. production response and alleged substantial levels of overproduction and export of U.S. upland cotton.

111. Third, Brazil asserts that the removal of the Step 2 program should be assessed as part of a “non-attribution” analysis and suggests that the original panel’s analysis somehow supports this approach. Brazil is wrong. The original panel never assessed the effects of Step 2 payments as part of any “non-attribution” analysis; Step 2 payments were, instead, part of the package of payments whose effects were *directly* at issue in the “present” serious prejudice analysis under Articles 5(c) and 6.3(c) of the *SCM Agreement*.

112. Nor does it make sense that *removal* of the Step 2 program would be part of a “non-attribution” analysis. As the Appellate Body has explained, a “non-attribution” analysis focuses on “ensur[ing] that the effects of other factors on prices are not improperly attributed to the challenged subsidies.”¹⁵⁸ This requires separating out the effects of other factors suppressing

¹⁵⁷ See U.S. First Written Submission, paras. 149-195; U.S. Rebuttal Submission, paras. 175-214; U.S. Oral Statement, paras. 54-59.

¹⁵⁸ *Upland Cotton (AB)*, para. 437. As the United States has noted in its prior submissions, Brazil has not made any meaningful attempt to “ensure that the effects of other factors on prices are not improperly attributed to the challenged subsidies.” *Upland Cotton (AB)*, para. 437. Brazil’s “analysis” consists of unsupported assertions that nothing “attenuates” the link that it asserts between the marketing loan and counter-cyclical payments and allegedly significantly suppressed world market prices. This is entirely insufficient to meet Brazil’s burden, especially in light of substantial evidence submitted by the United States (and even, unwittingly, by Brazil itself) showing the key importance of other factors (such as China’s trade in upland cotton) affecting world market prices. See *e.g.*, U.S. First Written Submission, paras. 308-318; U.S. Rebuttal Submission, paras. 387-396.

world market prices and ensuring that they are not attributed to marketing loan and counter-cyclical payments. As removal of the Step 2 program is not suppressing any prices, it is not logical to speak of including that factor in any “non-attribution” analysis.

2. Increase in world market share - Article 6.3(d) of the SCM Agreement

Questions to the United States

75. ***Could the United States explain further the textual basis of its argument that “Article 6.3(d) is not concerned with absolute market share and whether or not in any given year a member's market share would have been lower if subsidies were removed”? (Rebuttal Submission of the United States, para. 401)***

Questions to Brazil

76. ***What is the view of Brazil on the argument of the United States that an inquiry under Article 6.3(d) of the SCM Agreement requires two distinct elements: first, a demonstration of an increase in the world market share of a Member as compared to the average share it had during the previous period of three years, and, second, a demonstration that this increase in world market share compared to the average share the Member had during the previous period of three years is part of a consistent trend over a period when subsidies have been granted? (Rebuttal Submission of the United States, para. 399)***

113. The United States respectfully refers the Panel to its general comments above regarding Brazil's claims under Articles 5(c) and 6.3(d) of the *SCM Agreement* as well to the U.S. arguments on this issue in its prior submissions.¹⁵⁹

114. In its response to this question Brazil asserts that the second element of Article 6.3(d) – “this increase follows a consistent trend over a period when subsidies have been granted” – can be met simply by showing an increase in U.S. world market share from MY 1998 to MY 2005. Brazil's approach – if adopted – effectively write out of Article 6.3(d) both the reference to “this” increase and to a “consistent” trend.

115. As the United States explained in its answer to Question 75, Article 6.3(d) of the *SCM Agreement* is concerned with *increase* in world market share.¹⁶⁰ An *increase* is – by definition – “the action, process, or fact of making or becoming greater.”¹⁶¹ Thus, what is at issue in Article 6.3(d) is movement (“becoming greater”), not something static. The key question, then, is *what*

¹⁵⁹ See e.g., U.S. First Written Submission, paras. 323-343; U.S. Rebuttal Submission, paras. 399-404; U.S. Answers to Second Set of Panel Questions, paras. 171-172.

¹⁶⁰ U.S. Answers to Second Set of Panel Questions, paras. 171-172.

¹⁶¹ *The New Shorter Oxford English Dictionary* at 1350, Volume 1, (2002 Edition) (Exhibit US-148).

movement is relevant for purposes of that provision The text provides the answer. The movement that is relevant is that in getting from point A – “the average share [the allegedly subsidizing Member] had during the previous period of three years,” – to point B, the level in the year that is the subject of the claim. If upward movement – *i.e.*, “increase” or “growth” – is involved in getting from the former to the latter, and the upward movement is shown to be “the effect” of a challenged subsidy – the first element of Article 6.3(d) is satisfied.

116. An “increase” is also at issue in the second element of Article 6.3(d) – the requirement that “this increase” be shown to “follow[] a consistent trend over a period when subsidies have been granted.” Again, the text makes clear which particular increase is at issue – it is “this increase” – *i.e.*, the *same* increase that was relevant for purposes of the first element. Thus, under the second element, the complaining party must show that “this increase” – the “increase in the world market share it had during the previous period of three years” – “follows a consistent trend over a period when subsidies have been granted.”

117. Brazil’s argues that “the United States attempts to read the separate element of a three-year average into the element of a ‘consistent trend,’” but ignores the fact that Article 6.3(d) specifically refers to “this” increase, relating back to the reference to the increase over the previous three-year average. Brazil offers no reason why the drafters would have referred back to “this increase” if they had intended that a completely different increase – one defined by the complaining party – was to be the relevant increase for purposes of the second element of Article 6.3(d).

118. Instead, Brazil confuses two entirely separate questions. One question – just discussed – is what the relevant comparison is in assessing whether there has been an “increase” (*i.e.*, whether the proper points of comparison are the share of world production in a particular year versus the average share over the previous three-year period, as the text suggests, or rather two years selected by the complaining party, as Brazil urges). A second, and separate, question is whether an increase must be shown in *every* year in order to show that “this increase follows a *consistent trend* over a period when subsidies have been granted” (emphasis added). These are distinct issues. Contrary to Brazil’s assertions, the United States has never suggested that for a “consistent trend” to be shown there must be an increase in every single year that subsidies have been granted. Nor is this a necessary implication of the U.S. interpretation of Article 6.3(d).

119. While there may not be a need to show an increase in *every* year, where – as here – a complaining party can only point to one¹⁶² isolated year in which there has been an increase over the previous three-year average (and even that slight increase is shown to be both part of the ordinary fluctuation of world market share and caused by factors other than the challenged measures) there is clearly no basis whatsoever for an assertion of a “consistent trend.”

120. Indeed, it is Brazil’s interpretation that is inconsistent with the “consistent trend”

¹⁶² Or, at most two, if one considers world production plus beginning stocks.

language in Article 6.3(d). Brazil has argued that a complaining party should be able to satisfy the second element of Article 6.3(d) by simply selecting two end-points in the period that subsidies have been granted and drawing an upward-slanting line between the two points. However, this would simply show an increase. It would not necessarily show a “trend,” and it would most certainly not show a “consistent” trend. To the contrary, it would render the term “consistent” entirely meaningless because – under Brazil’s theory – there would only ever be two end-points and one line connecting them. This line could never be “consistent” with anything else because there would simply never be anything else with which to be “consistent.” Brazil would – in effect – simply write “consistent” out of Article 6.3(d) altogether. This is not an permissible interpretation of Article 6.3(d).

77. *In this connection, could Brazil respond to the argument of the United States that Brazil has not shown that either of these elements are met with respect to the marketing loan and counter-cyclical payment programs”? (Rebuttal Submission of the United States, paras. 399-403)*

121. The United States respectfully refers the Panel to its general comments above regarding Brazil’s claims under Articles 5(c) and 6.3(d) of the *SCM Agreement*, to the U.S. comments regarding Brazil’s answer to Question 76, as well to the U.S. arguments on this issue in its prior submissions.¹⁶³

C. CLAIM OF BRAZIL REGARDING THREAT OF SERIOUS PREJUDICE

Questions to both parties

78. *Could both parties comment on the statements of Canada that “(a)t issue is whether these programmes....threaten to cause serious prejudice simply by virtue of their existence” and that “(c)ertain subsidy programs, by their very nature, give rise to a constant likelihood of support that results in a permanent threat of serious prejudice”? (Third Party Submission of Canada, paras. 9-10)*

122. The United States respectfully refers the Panel to its general comments above regarding Brazil’s “threat of” serious prejudice claims under Articles 5(c) and 6.3(c) of the *SCM Agreement* as well to the U.S. arguments on this issue in its prior submissions.¹⁶⁴

79. *Could the parties state their views on the analysis of the ordinary meaning of the term “threat” in paras. 15-28 of the Third Party Submission of Canada?*

¹⁶³ See e.g., U.S. First Written Submission, paras. 323-343; U.S. Rebuttal Submission, paras. 399-404; U.S. Answers to Second Set of Panel Questions, paras. 171-172.

¹⁶⁴ See e.g., U.S. Rebuttal Submission, paras. 405-425; U.S. Answers to Second Set of Panel Questions, paras. 173-199.

123. The United States respectfully refers the Panel to its general comments above regarding Brazil's "threat of" serious prejudice claims under Articles 5(c) and 6.3(c) of the *SCM Agreement* as well to the U.S. arguments on this issue in its prior submissions.¹⁶⁵

Questions to the United States

80. *How does the United States address the argument of Japan that in view of the different purposes of Parts III and V of the SCM Agreement the standard for determining threat of material injury in Article 15.7 of the SCM Agreement is an inappropriate standard for determining the existence of a threat of serious prejudice under Part III of the SCM Agreement? (Third Party Submission of Japan, paras. 8-12.)*
81. *How does the United States respond to the argument of Australia that "it is beside the point for the United States to argue that the programmes under consideration are due to expire in late 2007"? (Third Participant Oral Statement of Australia, para. 13)*
82. *Could the United States comment on the projections of marketing loan and counter-cyclical payments in Table 26 of Brazil's First Written Submission and on the projections of prices and subsidy payments in Table 27 of Brazil's First Written Submission? Could the United States explain how the data in these Tables support its argument that producers are likely to expect low or no marketing loan payments in MY 2007? (Rebuttal Submission of the United States, para. 418)*

Questions to Brazil

83. *How does Brazil address the argument of the United States that footnote 13 of the SCM Agreement "does not indicate that where a panel finds that a Member is causing present serious prejudice through the use of a subsidy, the panel automatically also finds that the Member is threatening to cause serious prejudice in the future through the use of the same subsidy"? (Rebuttal Submission of the United States, footnote 624)*
84. *Could Brazil confirm that its claim of threat of serious prejudice is submitted on a contingent basis i.e., that it does not request the Panel to make a finding on this claim if the Panel make a finding of present serious prejudice? How is the contingent character of this "threat of serious prejudice" claim reflected in*

¹⁶⁵ See e.g., U.S. Rebuttal Submission, paras. 405-425; U.S. Answers to Second Set of Panel Questions, paras. 173-199.

Brazil's request for the establishment of a panel?

85. ***Could Brazil explain its request that the Panel "make factual findings with respect to its 'threat of serious prejudice' claim to allow the Appellate Body to complete the analysis, in case it were to disagree with the compliance panel's interpretation"? (First Written Submission of Brazil, para. 241) What are the precise "factual findings" which Brazil requests the Panel to make in this regard?***
86. ***How does Brazil address the argument of the United States that the definition of "threat" of injurious effects in Article 15.7 of the SCM Agreement and Article 4.1(b) of the Agreement on Safeguards "in terms of their close proximity in time and their high probability of occurring" reflects the ordinary meaning of the word "threat" and that, as such, Article 15.7 of the SCM Agreement and Article 4.1(b) of the Agreement on Safeguards provide "useful contextual guidance" for the interpretation of "threat" of serious prejudice?***

124. The United States respectfully refers the Panel to its general comments above regarding Brazil's "threat of" serious prejudice claims under Articles 5(c) and 6.3(c) of the *SCM Agreement* as well to the U.S. arguments on this issue in its prior submissions.¹⁶⁶ In addition, the United States submits the following observations regarding Brazil's answer to this question.

125. Article 3.2 of the DSU provides that "the dispute settlement system of the WTO . . . serves to . . . clarify the existing provisions of those agreements in accordance with customary rules of interpretation of public international law." One of these "customary rules" is that treaty terms are to be interpreted "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."¹⁶⁷ In its response to this question and Question 88, Brazil urges the Panel to ignore the U.S. application of this rule in interpreting the term "threat" in footnote 13. Brazil provides no basis for why Article 3.2 of the DSU should not be applied here.

126. As United States has explained, the ordinary meaning of the term "threat" includes *both* concepts of probability of occurrence and close proximity in time.¹⁶⁸ This is reflected in Articles 15.7 of the *SCM Agreement*, Article 3.7 of the Agreement on Implementation of Article VI of the

¹⁶⁶ See e.g., U.S. Rebuttal Submission, paras. 405-425; U.S. Answers to Second Set of Panel Questions, paras. 173-199.

¹⁶⁷ See *United States – Gasoline (AB)*, p. 17 (noting that "[this] general rule of interpretation [codified in Article 31 of the Vienna Convention on the Law of Treaties] has attained the status of a rule of customary or general international law. As such, it forms part of the 'customary rules of interpretation of public international law' which the Appellate Body has been directed, by Article 3(2) of the DSU, to apply in seeking to clarify the provisions of the General Agreement and the other 'covered agreements' of the Marrakesh Agreement Establishing the World Trade Organization. . . .")

¹⁶⁸ See U.S. Rebuttal Submission, para. 409.

General Agreement on Tariffs and Trade (“*AD Agreement*”), and Article 4.1(b) of the *Agreement on Safeguards* in describing the meaning of the term “threat.” By application of customary rules of treaty interpretation under Article 3.2 of the DSU, the ordinary meaning of “threat” of certain injurious effects as reflected in these other provisions provides important contextual guidance in interpreting “threat” of serious prejudice in Article 5(c)/footnote 13 of the *SCM Agreement*.

127. There is no merit to Brazil’s arguments that the Panel should artificially strip out the concept of close proximity in time from the ordinary meaning of “threat” in footnote 13 and should disregard the important contextual confirmation provided in the definition of “threat” in Articles 15.7 of the *SCM Agreement*, Article 3.7 of the *AD Agreement*, and Article 4.1(b) of the *Agreement on Safeguards*.

128. Brazil alleges, for example, that “Article 4.1(b) and 2 of the *Agreement on Safeguards* as well as Article 15.7 of the *SCM Agreement* deal primarily with the threat posed by a potential surge of imports” but that “[b]y contrast, Articles 5(c) and 6.3as well as footnote 13 of the *SCM Agreement* deal with the likelihood of adverse effects – not subsidized imports – occurring sometime in future.”¹⁶⁹ Brazil suggests that this is one reason why the concept of close proximity in time should be artificially stripped out of the ordinary meaning of “threat” for purposes of footnote 13. This argument is flawed.

129. First, it is wrong in its characterization of Article 15.7 of the *SCM Agreement*. Neither that provision – nor, for that matter its counterpart in Article 3.7 of the *AD Agreement* – “deal primarily with the threat posed by a potential surge of imports,” as Brazil suggests. To the contrary, Article 15.7 expressly states that it is concerned with the “threat of *material injury*,” not a “surge in imports.” A “surge in imports” is not even required for a showing of material injury. To the contrary, Article 15.7 identifies as only *one* of five factors that administering authorities “should” consider (“*inter alia*”) in making a “threat of material injury” determination whether there has been “a significant rate of increase of subsidized imports into the domestic market indicating the likelihood of substantially increased importation.” The chaussette to Article 15.7 even makes clear that “no one of [the five] factors by itself can necessarily give decisive guidance.” In other words, Article 15.7 of the *SCM Agreement* could hardly be more clear that it does *not* “deal primarily with the threat posed by a potential surge of imports.” Brazil’s arguments premised on that assertion are, thus, irrelevant.

130. Second, Brazil ignores the fact that “injury” is itself classified as an “adverse effect” under Article 5 of the *SCM Agreement*. Indeed, Article 5 of the *SCM Agreement* makes clear in footnote 11 that “injury to the domestic industry” therein is “used here in the same sense as it is used in Part V.” Thus, it is illogical for Brazil to assert that the focus in Article 5 on adverse *effects* somehow places a “threat of serious prejudice” inquiry into a fundamentally different category than a “threat of material injury” inquiry; one that precludes the Panel from consulting the ordinary meaning of “threat” in the latter context as important contextual guidance in

¹⁶⁹ Brazil Answers to Second Set of Panel Questions, para. 172.

interpreting the same word in footnote 13.

131. An inquiry into whether subsidized imports into the domestic market of a Member threaten to cause material injury is no less an inquiry into *effects* than an inquiry as to whether subsidies threaten to cause serious prejudice to the interests of another Member. The fact that one looks to the effects of subsidized imports while the other looks to the effects of subsidies is not material; the United States has never suggested that footnote 13 and Article 15.7 are identical provisions. And there is certainly no requirement that two provisions be identical in order for one to provide contextual guidance as to another.

132. Brazil also alleges that the Panel should read the concept of close proximity in time or “imminence” out of the ordinary meaning of the term “threat” in footnote 13 because the multilateral remedy available under Article 5 is somehow a “slow” remedy while the remedy available under Part V of the *SCM Agreement* is a “quick” remedy. Once again, the factual predicate of Brazil’s argument is flawed. A remedy in WTO dispute settlement is not necessarily any more “slow” or “fast” than the process of applying duties under the *SCM Agreement*, *AD Agreement*, or *Safeguards Agreement*. Indeed, the pace of a particular WTO, CVD, AD, or safeguard proceeding necessarily depends on the particular circumstances of each proceeding.

133. Investigations by different Members’ authorities require differing periods of time. And different Members may have different appeal mechanisms that affect the amount of time to obtain a remedy. In short, any number of factors could affect whether or not the domestic remedy available under the *SCM Agreement*, *AD Agreement*, and *Safeguards Agreements* is a slow or fast remedy. The same is true for the multilateral remedy available through WTO dispute settlement (e.g., the amount of time required for a remedy could depend on the complexity of the dispute brought by the complaining party, whether any appeals are made, the reasonable period of time for implementation of any adverse findings and other such factors). Brazil’s generic assertions about the “slowness” or “quickness” of the different remedies is, thus, speculative at best.

134. In any event, Brazil neglects one simple fact – the drafters *chose* to use the same term (“threat”) in all four contexts. If the remedies available thereunder were *so* different that same word could not even have the same ordinary meaning in the four contexts, the drafters could very well have chosen to use different words. They could very easily have inserted, for example, Brazil’s preferred “significant likelihood” standard in footnote 13 to differentiate it from “threat” in Articles 15.7 of the *SCM Agreement*, Article 3.7 of the *AD Agreement*, and Article 4.1(b) of the *Agreement on Safeguards*. But they did not do so. They chose to use “threat” in all four contexts and – for clarity – even expressly reflected the ordinary meaning of that term in certain of the provisions. Brazil has no basis unilaterally to change the text now.

87. *Could Brazil comment on the argument of the United States that the standard of “significant likelihood” is without support in the text of the SCM Agreement*

or in the GATT/WTO dispute settlement reports cited by Brazil? (Rebuttal Submission of the United States, paras. 406, 410,413)

135. The United States respectfully refers the Panel to its general comments above regarding Brazil's "threat of" serious prejudice claims under Articles 5(c) and 6.3(c) of the *SCM Agreement* as well to the U.S. arguments on this issue in its prior submissions.¹⁷⁰

88. *Does Brazil agree or disagree with the proposition advanced by the United States that "[a] panel may consider the ordinary meaning of a term as reflected in a particular provision to interpret the same term in another provision (especially of the same agreement) without the need for an express cross-reference." (Rebuttal Submission of the United States, para. 411, footnote 635)*

136. The United States respectfully refers the Panel to its general comments above regarding Brazil's "threat of" serious prejudice claims under Articles 5(c) and 6.3(c) of the *SCM Agreement*, to the U.S. comments regarding Brazil's answer to Question 86, as well to the U.S. arguments on this issue in its prior submissions.¹⁷¹

89. *Brazil argues that marketing loan and counter-cyclical payments for upland cotton are designed "in such a manner that payments would be made in consistently large amounts". (First Written Submission of Brazil, para. 270)*

(a) *Could Brazil in this regard discuss the data in Table 27 of Brazil's First Written Submission that show an increase in the projected farm price and AWP over the period MY 2006 - 2010 and a decline in projected marketing loan payments?*

(b) *How does Brazil respond to the argument of the United States that "by MY 2008, the projection is of no marketing loan payment at all"? (Rebuttal Submission of the United States, para. 419).*

137. The United States respectfully refers the Panel to its general comments above regarding Brazil's "threat of" serious prejudice claims under Articles 5(c) and 6.3(c) of the *SCM Agreement* as well to the U.S. arguments on this issue in its prior submissions.¹⁷²

138. In addition, the United States notes that, in its response to this question, Brazil attempts

¹⁷⁰ See e.g., U.S. Rebuttal Submission, paras. 405-425; U.S. Answers to Second Set of Panel Questions, paras. 173-199.

¹⁷¹ See e.g., U.S. Rebuttal Submission, paras. 405-425; U.S. Answers to Second Set of Panel Questions, paras. 173-199.

¹⁷² See e.g., U.S. Rebuttal Submission, paras. 405-425; U.S. Answers to Second Set of Panel Questions, paras. 173-199.

to explain away the evidence – submitted by Brazil itself – undermining its assertions that marketing loan payments are “designed ‘in such a manner that payments would be made in consistently large amounts.’” Table 27 submitted by Brazil in its own first written shows the AWP *increasing* over the period MY 2006-2010 and projected marketing loan payments *declining* over the same period. Brazil's response is, however, inexplicable.

139. Brazil delves into a discussion of “deterministic” versus “stochastic” projections of government outlays in its response to the Panel's question. However, according to Brazil's own notations, Table 27 presents, *inter alia*, the AWP and payments under the marketing loan and counter-cyclical payments projected by FAPRI. The total amount of government outlays shown in Table 27 were *not* projected by FAPRI; to the contrary, the government outlays were *estimated by Brazil*.¹⁷³ In any event, as USDA points out in the very document Brazil cites for the proposition that “deterministic projections, by their nature, tend to underestimate outlays”:

The Congressional Budget Office (CBO) and the *Food and Agricultural Policy Research Institute (FAPRI)* have used a stochastic approach to estimate outlays and cost legislative proposals for some time. CBO adopted a stochastic approach for crop sector analysis in September 1995 while working on the 1995/96 budget reconciliation/farm bill debate. *FAPRI* adopted a stochastic approach just prior to the 2002 farm bill debate.¹⁷⁴

140. Indeed, the July 2006 FAPRI baseline from which the data in Table 27 is taken is simply an update of the “full” 2006 baseline published earlier. The earlier baseline clarifies that “[i]n recent years, we have reported average values from the stochastic analysis for government costs and farm income and traditional point estimates for all other variables.”¹⁷⁵ Thus, the simple answer that Brazil fails to provide is that – at the time FAPRI issued its July 2006 baseline update FAPRI projected that in MY 2007 the marketing loan payment would be *less than one-half of a cent and thereafter would amount to nothing at all*. The very fact that the projection was made – projections that were considered sufficiently reliable for Brazil to include in its written submission and use in its modeling exercise – confirm that marketing loan program was not set up pursuant to some master “design” to result in large payments.

141. What the marketing loan program under the FSRI Act of 2002 *was* designed to do, moreover, was expire after MY 2007. Thus, regardless of whether projections are “deterministic” or “stochastic,” whether they are of \$1 or \$1 billion, the fact is *none of them take into account the fact that, as currently scheduled, no marketing loan payments will be made under the FSRI Act of 2002 in MY 2008*. That fact alone renders Brazil's claims moot to the

¹⁷³ See Brazil First Written Submission, Table 17, n. 454.

¹⁷⁴ Explanatory Notes for Stochastic Budget Outlays, (Exhibit BRA-460)

¹⁷⁵ FAPRI 2006 U.S. Baseline Briefing Book, p. 1 (available at http://www.fapri.missouri.edu/outreach/publications/2006/FAPRI_UMC_Report_01_06.pdf).

extent that they extend to any hypothetical measures in that year.

D. EXPORT CREDIT GUARANTEES

1. Outstanding export credit guarantees

Questions to the United States

90. *The United States states, in para. 50 of its Opening Statement, that:*

... nothing in the SCM Agreement provides that “withdrawing” a “subsidy” allegedly “taking the form of a program” “includes an obligation to abstain from performing on commitments outstanding under that program as of the deadline for implementation.” That argument improperly equates “performing on commitments under the program” with the “subsidy” itself. Such an equation was appropriate in Brazil – Aircraft (21.5), where Brazil continued to issue new WTO-inconsistent bonds even after the period of implementation on the basis that it had pre-existing contractual obligations to do so. However, it is not accurate here, where the guarantees are not themselves prohibited subsidies.

Would the United States please clarify what it meant in the underlined sentence?

91. *In paragraph 342 of its First Written Submission, Brazil indicates that the total amount of guarantees under the GSM 102, GSM 103 and SCGP programs outstanding on 1 July 2005 amounted to \$8.5 billion.*

- (a) Does the United States agree with the figure provided by Brazil?*
- (b) Please indicate what proportion of that amount concerns exports of unscheduled products? (please distinguish between principal and interests)*
- (c) Please indicate what proportion of that amount concerns exports of scheduled products, and in particular rice (please distinguish, in each case, between principal and interest).*

Questions to Brazil

92. *Is it of any relevance to the Panel's assessment of Brazil's claims concerning "outstanding" export credit guarantees that what was at issue in Brazil – Aircraft (21.5) was the issuance, after the implementation date, of new bonds, and that bonds which had been issued prior to the implementation date could be redeemed for a number of years thereafter (see para. 46 of the US' Opening Statement at the panel meeting).*

142. Contrary to Brazil's assertions, the situation in the present proceeding with respect to export credit guarantees issued prior to July 1, 2005 is not analogous to Brazil's continued provision of WTO-inconsistent bonds in *Brazil – Aircraft (21.5)*. Brazil's bonds continued to be prohibited export subsidies both before and after the date of implementation. By contrast, since July 1, 2005 (and, indeed, even before that time), U.S. export credit guarantees ceased being part of any program that is being operated at a "net cost to the government."¹⁷⁶ Thus, unlike Brazil, the United States has not attempted to continue providing prohibited export subsidies past the date of implementation.

93. *The Panel notes that Exhibit Bra-516 indicates outstanding amounts for GSM 5 as of 30 June 2006 rather than as of 30 June 2005 as indicated in footnote 523 of Brazil's First Written Submission. Please explain.*

2. Legal Bases for Brazil's export subsidies claims

Question to the United States

94. *The United States has noted that the original Panel's findings (that the export credit guarantees at issue constituted prohibited export subsidies) were based on item (j). The United States has also asserted that it has based itself on item (j) in implementing the DSB recommendations with respect to export credit guarantees. Please clarify whether the Panel should understand the United States' argument in this respect as an argument concerning the scope of the present proceeding.*

3. "Benefit" under Articles 1.1 and 3.1(a) of the SCM Agreement

Questions to both parties

95. *Brazil has taken the position that "different parties to a transaction involving a GSM 102 ECG derive different benefits from the GSM 102 ECG, each of which is potentially subject to assessment under Article 1.1(b) of the SCM*

¹⁷⁶ *Upland Cotton (Panel)*, para. 7.804.

Agreement” and has indicated that it is, in this proceeding, “primarily concerned” with the benefit received by the US exporter in the form of below-market fees (para. 404, Brazil's Rebuttal). The United States has challenged Brazil's approach of focusing on fees to the exclusion of other elements of the total cost of the loan. Please explain, referring to the provisions of the SCM Agreement and WTO jurisprudence (if any applicable), your position as to whether: (1) export credit guarantees and other types of subsidies may involve more than one type of benefit and/or recipient; (2) whether it is up to the complaining Member to decide which benefit it chooses to challenge.

143. The United States respectfully refers the Panel to the U.S. response to this question.¹⁷⁷ In addition, the United States offers the following observation regarding Brazil's response.

144. Brazil's response assumes that the United States “argues that Brazil must prove that [an export credit] guarantee also resulted in a benefit to a foreign bank by lowering the ‘total cost of funds’ involved in the transaction.”¹⁷⁸ This is a mischaracterization of the U.S. position. The United States has made no argument concerning the necessity to prove a benefit to any particular participant in a transaction or group of participants. Instead, consistent with Article 14(c) of the *SCM Agreement*, the United States has argued that the proper focus is on the guaranteed loan transaction itself, and whether there is a “difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee.”

145. The express focus under the text is on a comparison of two *transactions* to determine whether a benefit exists at all, not on whether a particular entity does or does not receive a benefit. Brazil has made no attempt to provide such specific information on individual loan costs and fees or to identify comparable commercial loans and their terms.

96. *The parties differ as to whether different types of loans can be compared as long as they have the same "average life." What support (economic literature, etc.) exists for your position on this issue?*

146. Brazil's response to this question appears to be irrelevant to the question posed by the Panel. Brazil offers an exhibit (BRA-686) in which the consultant retained by Brazil for purposes of this dispute expounds on “why at any point in time, the principal exposures between the two-year bullet loan and the three-year amortizing loan can be different.”¹⁷⁹ However, the United States has never argued that a loan with principal payable over 3 years has the same principal exposure as a loan with principal payable over 2 years. To the contrary, the United

¹⁷⁷ U.S. Answers to Second Set of Panel Questions, paras. 206-211.

¹⁷⁸ Brazil Answers to Second Set of Questions, para. 203

¹⁷⁹ Brazil Answers to Second Set of Questions, para. 225.

States has simply demonstrated that the prosaic arithmetic concept of average life provides a common and straightforward basis for comparing the costs and fees derived for loans of differing principal repayment terms.¹⁸⁰

147. Brazil has previously argued that such a difference *necessarily* renders the two types of loans not comparable because “the patterns of credit risk to which the lender is exposed are very different in these two cases.”¹⁸¹ Brazil now appears to retreat from this unequivocal argument, when it states that the difference in principal repayment terms “pose *potentially* differing risks of default.”¹⁸²

148. Brazil's consultant states “the likelihood of default in the two periods *may* be different.”¹⁸³ Presumably, therefore, they may also *not* be different. As the United States has previously observed, Brazil's analysis simply *assumes*, without a factual basis, “that the borrowing bank's credit outlook is sufficiently positive in the short term that there is a very low default likelihood perceived in the first two years . . . and a greater likelihood of default in the third year.”¹⁸⁴

149. Brazil's consultant expressly acknowledges that if the chance of default in each of the years is the same then there is no difference in spread between the two-year bullet loan and the three-year amortized loan.¹⁸⁵ However, he argues that if one assumes the risk of default is higher after the first year then “the amortizing loan commands a higher spread.”¹⁸⁶ And, conversely, if one assumes higher risk of default in the first year, “the amortizing loan now has a lower spread.”¹⁸⁷ While this may be true, in the absence of any factual basis in the examples before the Panel for an assumption that the risk is greater in the out years, then Brazil's theoretical disquisition is of no significance. Far from there being any such factual basis, however, the United States has actually submitted evidence that in a study of medium-term U.S. government-guaranteed loans, the authors found that “as the medium-maturity loans season the likelihood of default increases initially, peaks in the second year after origination, and declines thereafter.”¹⁸⁸

¹⁸⁰ U.S. First Written Submission, paras. 123-124; U.S. Rebuttal Submission, para. 153; U.S. Answers to Second Set of Panel Questions, paras. 212-218.

¹⁸¹ Rebuttal Submission of Brazil, para. 429; *see also*, Oral Statement of Brazil, para. 219; Brazil's Comments on U.S. Answers, para. 140.

¹⁸² Brazil Answers to Second Set of Questions, para. 225.

¹⁸³ Brazil Answers to Second Set of Questions, Exhibit Bra-686, para. 11.

¹⁸⁴ Oral Statement of Brazil, para. 220.

¹⁸⁵ Brazil Answers to Second Set of Questions, Exhibit Bra-686, para. 30.

¹⁸⁶ Brazil Answers to Second Set of Questions, Exhibit Bra-686, para. 31.

¹⁸⁷ Brazil Answers to Second Set of Questions, Exhibit Bra-686, para. 31.

¹⁸⁸ Glennon, Dennis and Nigro, Peter; “Measuring the Default Risk of Small Business Loans: A Survival Analysis Approach,” *Journal of Money, Credit, and Banking*, Vol. 37, No. 5 (October 2005), pp. 945 (Exhibit US-152).

150. In any event, in the absence of any specific basis for assigning, in particular transactions, differing default risks in particular years, Brazil's analysis simply *confirms* the basic utility of average life for comparing pricing of loans of different principal repayment terms.

Questions to the United States

97. *Assuming that the Panel accepts the United States' argument that "benefit" is to be assessed on the basis of the "total costs of funds," what do you consider Brazil must establish in order to meet its burden of proof in that respect? Must Brazil prove that a benefit is conferred in all instances (all transactions and all recipients)? In most instances?*
98. *Does the United States dispute the accuracy of Brazil's comparison of GSM 102 fees with Exim Bank fees? Does the United States agree that ExIm Bank and GSM 102 guarantees are (at least in certain circumstances) similar or comparable?*
99. *Please comment on Brazil's argument that the GSM 102 fees are not sufficiently scaled to take into account country risk (i.e. they vary only minimally according with country risk) (see, inter alia, paras. 410-412 Brazil's First Written Submission).*

Questions to Brazil

100. *Assuming the Panel were to agree with the United States that the proper benchmark to determine "benefit" is the "total cost of funds" of the transactions, what elements of evidence has Brazil provided the Panel in this respect (other than evidence from the Regulations that the programme targets situations where no credit would be available on the market)? In answering, please address the United States' argument at para. 133 of its First Written Submission that "Brazil has made no attempt to provide such specific information on individual loan costs and fees or to identify comparable commercial loans and their terms".*

151. Effectively conceding that it has not provided the requisite specific information on loan costs and fees or identified comparable commercial loans and their terms, Brazil protests that it is "not in the position of an investigating authority" and therefore cannot be expected to produce "this type of data."¹⁸⁹ This does not excuse Brazil from making a *prima facie* case of breach. If

¹⁸⁹ Brazil Answer to Question 100, para. 226. Brazil later asserts that it has discharged its burden by virtue of its "ExIm Bank fee comparison." *Id.*, para. 244. This comparison of fees is not an appropriate analysis. Moreover, the United States has demonstrated, however, the elements of the Ex-Im Bank products render them not comparable to the GSM-102 guarantee. U.S. Answer to Question 98 (2 April 2007).

it does not have evidence that the United States is breaching its WTO obligations – as the United States has argued is in fact the case – Brazil has no basis to make claims to that effect before a WTO panel. Brazil finds itself in no different position than domestic industries, who must submit sufficient evidence of subsidization (including financial contribution, benefit, and specificity within the meaning of Articles 1 and 2 of the *SCM Agreement*) and injury in order to warrant an investigation under Part V of the *SCM Agreement*.

152. Brazil next implies that the commercial bank that has provided specific transactional information submitted by the United States may be motivated to falsify such information because of a specific interest in maintaining the GSM 102 program.¹⁹⁰ These assertions are completely baseless and do not merit a response.

153. Brazil also mischaracterizes the arguments of the United States. Brazil asserts that “the United States argues, in essence, that the interest that the lender charges on a loan guaranteed by the U.S. government could be higher than the interest it charges on a loan guaranteed by a commercial enterprise.”¹⁹¹ Consistent with Article 14(c) of the *SCM Agreement*, however, the arguments of the United States have not been restricted to comparisons of interest alone, nor to a comparison of two transactions in which a guarantee is necessarily involved. Rather, the United States has noted that private sector commercial products comparable to the GSM-102 program are available in the marketplace and commercial lenders have provided unsecured financing to foreign banks who are CCC-approved obligors on terms the annualized cost of which was less than that available under the GSM-102 program.¹⁹² This contradicts Brazil's sweeping assertions that GSM 102 guarantees are only provided where credit would not otherwise not have been available to foreign obligors.

154. Finally, Brazil asserts that “as a factual matter, [] Article 14(c) is not directly applicable to GSM 102.”¹⁹³ The United States has never asserted that Article 14(c) is directly applicable. Rather, the United States – like the Appellate Body – has noted that Article 14 provides key contextual guidance in assessing “benefit.” In the case of loan guarantees, it is Article 14(c) that is relevant.

155. Article 14(c) recognizes that a loan guarantee is made for the sole purpose of supporting a loan transaction; the guarantee becomes an integral part of that transaction and has no value beyond it. The particular fee assessed for a guarantee is affected by the terms of the underlying loan transaction, who the parties are to the underlying loan transaction, the nature of the goods being purchased and sold, and any number of other factors. In turn, the terms of the underlying loan transaction and the costs and fees associated with that financing may be affected by the fees

¹⁹⁰ Brazil Answers to Second Set of Questions, para. 226 and fn. 297.

¹⁹¹ Brazil Answers to Second Set of Questions, para. 246.

¹⁹² See, e.g., U.S. First Written Submission, paras. 111-131

¹⁹³ Brazil Answers to Second Set of Questions, para. 234.

assessed.

156. Therefore, the drafters expressly provided that “a loan guarantee by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee. In this case the benefit shall be the difference between these two amounts adjusted for any differences in fees.” In other words, they expressly recognized that an assessment of the total costs of the transaction is necessary to assess whether a “benefit” is *actually* conferred by the guarantee. Brazil has provided no basis to depart from this logic,

101. Brazil argues that “[w]here guarantees are reserved for circumstances in which credit would not otherwise be available, there is no “comparable commercial loan absent the government guarantee,” within the meaning of Article 14(c) of the SCM Agreement.” (Brazil First Written Submission, para. 375). The Panel understands this argument of Brazil to focus on the foreign obligor. Brazil elsewhere indicates that it is principally concerned, in this proceeding, with the benefit to the US exporter (fees). Are these two arguments at tension?

4. Item (j) of the Illustrative List

Questions to both parties

102. What, in your view, explains the different results achieved by the two methods advocated, on the one side, by the United States in paragraphs 87-89 of its First Written Submission and by Brazil in Exhibit Bra-613 (other than the United States’ criticism that Brazil has not taken recoveries corresponding to pre-1992 guarantees into account in its “cash basis” accounting calculations, of which the Panel is already aware)?

157. The United States appreciates the observation by Brazil that under the Federal credit reform accounting methodology, “application of re-estimates effectively converts the process to a retrospective, cash-basis accounting methodology.”¹⁹⁴ It is precisely because of such re-estimates that the profitability of the export credit guarantee programs is evident.¹⁹⁵ As Brazil elsewhere notes in its answers to the Panel’s questions, the required accounting methodology under the Credit Reform Act of 1990, “measure[s] more accurately the costs of Federal credit programs’ than does cash-basis accounting.”¹⁹⁶

158. In addition to this observation, the United States respectfully refers the Panel to its

¹⁹⁴ Brazil Answers to Second Set of Questions, para. 266.

¹⁹⁵ See, e.g., U.S. First Written Submission, paras. 81-99.

¹⁹⁶ Brazil Answers to Second Set of Questions, paras. 273, 285.

extensive arguments regarding the profitability of the export credit guarantee programs in its prior submissions.¹⁹⁷

103. To what extent is evidence pertaining to guarantees issued under the three programmes (GSM 102, GSM 103 and SCGP) under the prior fee schedule relevant to the Panel's analysis of the revised GSM 102 programme under item (j)?

159. The United States has already addressed all of Brazil's arguments in response to this question in its prior submissions. Brazil is simply incorrect to assert that CCC "predicts" that "'cohorts' of GSM 102 ECGs issued in FY 2006 and FY 2007 (and thus under the amended GSM 102 fee schedule) will suffer losses over the long term."¹⁹⁸ In this respect, the United States respectfully refers the Panel to the U.S. comments on Brazil's answer to Question 105 below as well as the U.S. Rebuttal Submission at paragraphs 108-126. With respect to the "cash results" that Brazil advances,¹⁹⁹ the United States respectfully refers the Panel to the U.S. comments herein in response to Brazil's answers to Question 102 and 106.

104. Must a risk-based fee necessarily take into account foreign obligor risk? Please discuss and provide any relevant support for your position. Can foreign obligor risk be treated differently than country risk in this respect, and if so, why?

160. The United States respectfully refers the Panel to its own response to Question 104²⁰⁰ and simply notes again that it establishes internal bank limits to govern exposure to potential defaults by foreign obligor banks in individual transactions.²⁰¹ Brazil does not dispute the fact of such limits but indicates that the United States has offered "no evidence" of the way in which it establishes such limits. In particular, Brazil suggests that "CCC does not account for differing ratings between individual non-sovereign foreign obligors in a country, [but] rather, it applies a single rating . . . for all non-sovereign foreign obligors within that country."²⁰² Brazil is incorrect.

161. As the United States has explained, CCC conducts an independent analysis of *each* foreign bank to establish the risk rating for such bank and the resulting bank limit.²⁰³ The Office of Management and Budget ("OMB") establishes 11 sovereign and 9 non-sovereign risk categories for use by government agencies and programs subject to the Federal Credit Reform

¹⁹⁷ See e.g., U.S. First Written Submission, paras. 73-104; U.S. Rebuttal Submission, paras. 84-100.

¹⁹⁸ Brazil Answers to Second Set of Questions, para. 272.

¹⁹⁹ Brazil Answers to Second Set of Questions, paras. 276-278.

²⁰⁰ U.S. Answers to Second Set of Panel Questions, paras. 246-248.

²⁰¹ U.S. First Written Submission, para. 78.

²⁰² Brazil Answers to Second Set of Questions, para. 281

²⁰³ U.S. First Written Submission, para. 78

Act of 1990.²⁰⁴ CCC uses the same risk category methodology to classify foreign banks it approves for the GSM-102 program. Generally, if a bank is itself considered to be sovereign, then it will not be rated better than the sovereign country rating. Similarly, if a bank is considered non-sovereign, then it generally will not be rated better than the OMB non-sovereign rating for its country. CCC's independent analysis of each bank applies a standard CAMEL approach, evaluating capital adequacy, asset quality, management, earnings, and liquidity of the foreign bank.²⁰⁵

105. What considerations must guide the Panel's decision to accept or refuse new evidence or arguments on issues that were addressed by the original Panel? Please discuss in light of the following:

- (a) ***The original Panel found that original subsidy estimates, while not reflecting 'actual' figures, nevertheless provide a reliable measure of the United States government's own assessment of the profitability of the export credit guarantee programmes. Is the United States asking the Panel to revisit that conclusion (see paras 108 ff. of the United States' First Written Submission).***
- (b) ***The United States presents evidence which, it argues, demonstrates that the three programmes examined by the original panel were operated at no net cost to the US government. Is there any issue as to whether the Panel can or should accept the United States' evidence in this respect?***

162. First, Brazil is incorrect to assert that “the CCC predicts that costs and losses for the ‘cohorts’ of GSM 102 ECGs newly issued in FY 2006, FY 2007 and FY 2008 will, over the long term, exceed fees, penalties and recoveries.”²⁰⁶ As the United States has explained, initial subsidy estimates in the U.S. budget are not derived from the specific experience of the CCC programs, nor do they in any way constitute a prediction of loss.²⁰⁷

163. Furthermore, the United States does not “ask the compliance Panel to ignore the original panel and the Appellate Body’s findings” nor abandon “the original panel and Appellate Body’s adoption of a forward-looking, future-oriented assessment under a methodology ‘used and relied upon by the United States government to assess the estimated long-term net cost to the United States government of export credit guarantees,’ in favor of a purely retrospective assessment of

²⁰⁴ U.S. First Written Submission, para. 78, fn. 120; U.S. Rebuttal Submission, para.118; “Informal consultation questions to the United States,” question 19 (Exhibit BRA-517).

²⁰⁵ U.S. First Written Submission, para. 78, fn. 120; U.S. Answers to Second Set of Panel Questions, para. 248, fn. 266 and 279-283

²⁰⁶ Brazil Answers to Second Set of Questions, para. 284

²⁰⁷ U.S. Rebuttal Submission, paras. 108-126

program performance.”²⁰⁸ To the contrary, the United States has expounded at length on the prospective viability of the program²⁰⁹ and – unlike Brazil – on its profitability under the credit reform methodology “used and relied upon by the United States government.”²¹⁰

164. One additional factual assertion in Brazil's answer to Question 105 merits response. Brazil ascribes erroneous significance to “the USDA model” to which it refers in paragraph 302 of its answers and in Exhibit Bra-588. This is not a reference to a model specific to USDA of “expected loss rates or estimated default costs” particular to the CCC export credit guarantee programs, as Brazil asserts. Instead, it refers only to a cash flow model required of all U.S. government agencies providing international credit, which cash flow model is only an initial step in the budgetary process and which must, in any event, use risk ratings and assumed loss rates required by the OMB for all such agencies, irrespective of the particular program experience.²¹¹ The OMB then also requires such agencies to use “a credit subsidy calculator . . . that agencies use to convert agency-estimated cash flows into present values.”²¹² These figures can in no way be characterized to reflect that “CCC anticipates losses.”²¹³

106. *The parties disagree as to whether Brazil should include recoveries for pre-1992 guarantees in its cash basis accounting formula (Exhibit Bra-613). Is the Panel correct in understanding that Brazil's formula does not include amounts for (1) claims paid after 1992 under pre-1992 guarantees; (2) fees paid on pre-1992 guarantees? If so, please explain the relevance or non-relevance of including recoveries under pre-1992 guarantees in light of the non-inclusion of costs and other revenues related to the same guarantees.*

²⁰⁸ Brazil Answers to Second Set of Questions, para. 292

²⁰⁹ See, e.g., U.S. First Written Submission, paras. 73-80; U.S. Rebuttal Submission, paras. 101-107, 127-128

²¹⁰ See, e.g., U.S. First Written Submission, paras.81-99;U.S. Rebuttal Submission, paras. 84-100

²¹¹ United States Government Accountability Office Report to Congressional Committees (GAO-04-531) September 2004: Export Import Bank - OMB's Method for Estimating Bank's Loss Rates Involves Challenges and Lacks Transparency, p. 7 (Exhibit US-73) (“To estimate their subsidy costs, credit agencies estimate the future performance of direct and guaranteed loans. Agency management is responsible for accumulating relevant, sufficient, and reliable data on which to base these estimates. To estimate future loan performance, agencies generally have cash flow models, or computer-based spreadsheets, that include assumptions about defaults, prepayments, recoveries, and the timing of these events and are based on the nature of their own credit program. Agencies that provide credit to domestic borrowers generally develop these cash flow assumptions, which OMB reviews, based on their historical experience. *For U.S. international credits, OMB provides the expected loss rates, which are composed of default and recovery assumptions, that agencies should use to estimate their subsidy costs.*”) (Emphasis added)

²¹² United States Government Accountability Office Report to Congressional Committees (GAO-04-531) September 2004: Export Import Bank - OMB's Method for Estimating Bank's Loss Rates Involves Challenges and Lacks Transparency, p. 10 (Exhibit US-73).

²¹³ Brazil Answers to Second Set of Questions, para. 302

165. The United States respectfully refers the Panel to its own response to this question²¹⁴ as well as to the comments of the United States below in response to Brazil's answer to Question 114.

Questions to the United States

107. *What can explain the discrepancy between the "credit guarantee liability" recorded in the CCC's financial statements (which suggest that the program is provided at a net cost to the US government) and the evidence presented by the US in para. 87 of its First Written Submission?*
108. *Please explain why the "liability" figure in the CCC's financial statements should not be considered by the panel to provide, if not the amount of actual losses, at least a reliable estimate of the CCC's own perception of the cost to the government of the programmes since their inception. Is the Panel wrong in understanding that a "credit guarantee liability" in this context means that the CCC considers that the programmes will not cover their costs and losses in the long term?*
109. *Please indicate to the Panel whether there have been occurrences of reschedulings prior to the occurrence of defaults and the payment of claims by the CCC.*
110. *Is it possible to calculate the "subsidy estimate net of reestimates" for GSM 102 alone (similar to what the US has done for all three programmes in para. 87)? If so, please provide a table recording the results of this exercise.*
111. *In paragraph 7.853, the original Panel stated that it "disagree(d) with the United States that we should 'eliminate' the data for certain, more recent, cohorts in our analysis." Is the United States asking that this Panel eliminate such data for the most recent cohorts (the table at para. 87 of the United States' First Written Submission includes data up to 2005 only). Why should this Panel do what the original refused to do? What would be the result of the United States "re-estimates" exercise if the original subsidy estimate for the 2006 and 2007 cohorts were included?*
112. *Please explain whether and how the CCC limits risks or control costs of the GSM 102 programme as regards foreign banks' individual credit ratings.*

²¹⁴ The United States notes a typographical error in its response, however. In paragraph 261, the fourth sentence should read: "Therefore, it is inexplicable - and entirely disingenuous - that Brazil criticizes the United States for including recoveries received before 1992 (indeed as far back as 1980)." The United States inadvertently included "not" before "including" in its response.

113. Please explain whether and how CCC country risk categories correspond to ICRAS ratings.

Question to Brazil

114. Brazil argues that “(t)hat the United States has, on one view of the data, beaten the odds and met its costs and losses over a series of years does not mean that ECG programs are structured and designed to do so” (para. 503, Brazil's Rebuttal). Is Brazil arguing that evidence regarding the actual operation and “profitability” of the programme (i.e. retrospective evidence) is irrelevant to the Panel's analysis under item (j)?

166. The United States notes that Brazil now appears to be advocating exclusively for “cash results” in respect of an analysis under item (j).²¹⁵ This appears to be a *wholesale abandonment of Brazil's position in the original panel proceeding* regarding the credit reform accounting methodology, a shift that can only be explained by the fact that the methodology now confirms the robust profitability of the programs, directly undermining Brazil's theory in the present proceeding. The United States recalls that Brazil had previously stated that “it does *not* intend for this revised constructed formula to *replace* the formula used by the U.S. government itself to track the costs of the CCC guarantee programs pursuant to the U.S. Federal Credit Reform Act.”²¹⁶ Brazil's response to the compliance panel's Question 114 reflects a complete reversal of that position.

167. While Brazil's positions on the issue may shift to accommodate the results Brazil prefers, the overwhelming evidence confirms the profitability of the export credit guarantee programs. This evidence directly contradicts Brazil's claims that premiums charged under these programs are insufficient to cover the long-term costs and losses of the programs.

²¹⁵ Brazil Answers to Second Set of Questions, para. 314.

²¹⁶ Brazil's Answers to Questions Posed by the Panel Following the First Substantive Meeting of the Panel, para. 164 (Question 77) (11 August 2003) (emphasis in original)