

THE NEVER ENDING AGRICULTURAL TRADE LIBERALIZATION: THREE SUBSTANTIAL PROBLEMS*

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ABSTRACT

Agricultural Trade Liberalization has been one of the most controversial issues in International Trade. The conservative position assumed by WTO Members regarding the trade liberalization of agricultural barriers is rooted, amongst other reason, on the fact that countries do not want to depend on other governments for food (National Security). Due to the special treatment that countries give to agricultural goods, WTO Members negotiated in the Uruguay Round a separate agreement for agricultural trade, tailor-made for these goods, with an specific object and purpose: establish a fair and market-oriented agricultural trade policy.

Fecha de recepción: 2 de mayo de 2006
Fecha de aceptación: 5 de mayo de 2006

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The Agreement on Agriculture is built upon three pillars on into which WTO Members made commitments to reduce market protection. Accordingly, members made commitments on the areas of market access, domestic support and export subsidies. Since domestic support and export subsidies is nowadays one of the most controversial subjects when talking about international trade, this article will focus exclusively on this two issues, including both its regulation, and effects.

Regarding Domestic Support Measures, the Agreement on Agriculture classified different types of support as “Boxes”. The first type of support are Green Box Measures” which include all those domestic support payments that are deemed to have no or at most minimal trade distorting effects; “Amber Box Measures” which are those measures that do have trade distorting effects, and thus Members are bound to reduce these kinds of payments. Finally, Blue Box Measures, which are direct payments made under production limiting programs not subject to reduction commitments. Regarding Export Subsidies, the Agreement on Agriculture constitutes an exception to the general regime included in the Subsidies and Countervailing Measures Agreement (hereinafter SCM), as it allows Members to grant export subsidies provided that they comply both with their budgetary outlays and quantity commitment levels. Moreover, it prevents agricultural export subsidies from being challenged under SCM provisions if they caused adverse effects to the interests of other Members.

Even though the Agreement on Agriculture constitutes a significant breakthrough regarding agricultural trade liberalization, there are still some issues that erode the purpose of establishing a fair and market oriented agricultural trade policy.

The first problem arises with the expiration of the Peace Clause, which poses the question whether Members are able to challenge agricultural export subsidies under SCM provisions when the subsidy causes adverse effects to the interests of

another WTO Member; or if Members are going to continue protected from claims under the SCM Agreement even if their measures cause trade distorting effects. The second problem that the Agreement on Agriculture fails to address is that Members are able to disguise export subsidies within domestic support schemes. Finally, the third problem refers to how blue box subsidies cause trade distorting effects as much as amber box measures.

This article will present the existing problems in agricultural trade liberalization within the frame of the WTO. Subsequently it will show a hypothetical WTO case that includes the above-mentioned problems in agriculture nowadays and it will address a possible solution to the case for both the Claimant and Defendant parties. Finally, it will propose a solution to stop these problems that do not allow agricultural trade to be fair and market oriented.

Key words: Agreement on Agriculture, Domestic Support, Export Subsidies, Peace Clause, Blue Box Measures, Green Box Measures, Amber Box Measures, Serious Prejudice, Incorporated Products.

TRES PROBLEMAS SIGNIFICATIVOS
DENTRO DE LA APERTURA AGRÍCOLA
MULTILATERAL:
UNA MISIÓN QUE NUNCA ACABARÁ

RESUMEN

El tratamiento que se le da a la agricultura dentro de la globalización ha sido uno de los temas de mayor complejidad en el comercio internacional. La posición conservadora asumida por varios miembros de la Organización Mundial

del Comercio (OMC) al momento de desmontar las barreras agrícolas se explica, entre otras razones, por el hecho que los países no desean que la alimentación de su gente dependa de otros gobiernos (seguridad nacional). Debido al trato especial que los países le dan a los bienes agrícolas, los miembros de la OMC negociaron en la Ronda de Uruguay el denominado Acuerdo de Agricultura, diseñado a la medida de estos productos, pero con un objetivo y propósito específico: establecer un sistema de comercio agropecuario equitativo y orientado al mercado.

El Acuerdo de Agricultura está constituido sobre tres pilares básicos en los que los países parte decidieron reducir su protección a los mercados. Los miembros efectuaron compromisos en el área de acceso a mercados, apoyo interno, y subsidios a la exportación. El presente artículo analizará exclusivamente las últimas dos áreas, junto con su regulación y efectos, ya que a lo largo de la implementación del acuerdo han demostrado ser las más sensibles y controvertidas dentro del comercio internacional.

El Acuerdo de Agricultura clasificó las medidas de apoyo interno dentro de unas “cajas”. Un primer tipo de este apoyo son las “Medidas de caja verde”, las cuales se caracterizan por no tener efectos de distorsión del comercio ni efectos en la producción, o, a lo sumo, tenerlos en grado mínimo. En segundo lugar, las medidas de “Caja ámbar” son aquellas que tienen efectos de distorsión en el mercado y que por tanto están sujetas a los compromisos de reducción establecidos en el acuerdo. Por último, las medidas de “Caja azul” son pagos directos realizados en el marco de programas de limitación de la producción. Estos pagos no están sujetos a compromisos de reducción. En lo referente a subsidios a la exportación, el Acuerdo de Agricultura se constituye en una excepción frente a lo estipulado en el Acuerdo sobre subvenciones y medidas compensatorias (ASMC). El Acuerdo de Agricultura permite que los países miembros otorguen subsidios a la exportación

bajo el supuesto que cumplan con los compromisos de reducción. Adicionalmente, previene que dichos subsidios sean recurribles bajo las provisiones del ASMC si causan perjuicio grave a los países miembros.

Si bien es cierto que el Acuerdo de Agricultura constituye un avance significativo en la apertura del sector agrícola, aún continúan situaciones que atentan contra el propósito de lograr un sistema de comercio agropecuario equitativo y orientado al mercado. El primer problema surge con la expiración de la llamada Cláusula de paz, la cual establece la pregunta sobre si los subsidios a la exportación agrícolas pueden ser recurribles con relación a las reglas del ASMC si causan lo que se ha denominado perjuicio grave, o si por el contrario, dichos subsidios están blindados frente al ASMC. Un segundo problema se manifiesta en la forma como los países miembros disfrazan sus subsidios a la exportación dentro de esquemas de apoyo interno. Un tercer problema se refleja en los llamados Subsidios de caja azul, los cuales no están sujetos a compromisos de reducción y sin embargo pueden generar efectos de distorsión similares a los causados por las medidas de Caja ámbar.

Este artículo presentará los problemas relativos a la apertura del sector agrícola dentro del marco de la OMC. Posteriormente, mostrará un caso hipotético dentro del sistema de resolución de disputas de la OMC en donde se exponen los problemas agrícolas actuales, y presentará una solución a dicho caso dentro de la perspectiva de la parte recurrente y defendida. Finalmente, propondrá una solución que permitirá lograr desarrollar una política internacional encaminada a establecer un sistema de comercio agropecuario equitativo y orientado al mercado.

Palabras clave: acuerdo sobre agricultura, ayudas internas, subsidios a la exportación, cláusula de paz, medidas de caja azul, medidas de caja verde, medidas de caja ámbar, perjuicio serio, productos incorporados.

SUMMARY

I. Preface

II. Introduction

III. Three problems of the agreement on agriculture with respect to subsidies.

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“Agricultural support policies are costly to the countries applying them and they reduce the benefits from global economic activity. However, once established, they are difficult to remove...”¹.

I. PREFACE

This document is based on the written submission presented by the Pontificia Universidad Javeriana in the *Elsa Moot Court Competition On World Trade Organization Law* that took place in Geneva, in April 2006. The written submission won the *Cambridge University Press Award* for the Overall Best Memorial of the Competition.

The team representing the Pontificia Universidad Javeriana, integrated by the authors and Mr. GONZALO GUZMÁN CARRASCO

1 RAJ BHALA, *Internacional Trade Law: Theory and Practice*, Second edition, Lexis Publishing, 2001, p. 713.

(Advisor Professor), won the Latin American regional round in the WTO Moot Court that took place in Ciudad de Guatemala in March 2006, winning thereby the right to represent Latin America in the final Round of the Competition in Switzerland.

II. INTRODUCTION

Agricultural Trade Policy is one of the most complex issues in International Trade Law as it involves national security concerns, “multifunctionality” matters and political tensions². Accordingly, during the Uruguay Round negotiations countries decided to create a separate agreement with specific provisions on agricultural goods, with the aim of establishing a “fair and market-oriented Agricultural trading system” in an ongoing process³. However, the achievement of this goal has been eroded by the fact that Members have used ambiguous and deficient provisions of the Agreement on Agriculture (hereinafter AoA) to sustain conducts that disregard the main objective of liberalizing trade on agricultural products.

Forces underlying agricultural matters influence the position of WTO Members when it comes to negotiate trade liberalization. National security is the first force that prevents countries from opening agricultural markets, as they believe that self-sufficiency in agricultural production prevents dependence on other countries for food, something that precludes the risk of political subservience⁴. Additionally, Members justify agricultural protection adducing that it provides benefits other than trade, such as environmental values

2 MELAKU GEBOYE DESTA, “The Bumpy Ride Towards the Establishment of a “Fair and Market Oriented Agricultural Trading System” at the WTO: Reflections Following the Cancun Setback”, *Drake Journal of Agricultural Law*, Fall 2003, p. 493.

3 Agreement on Agriculture of 15 April 1994, LT/UR/A-1/2, Preamble.

4 JEFFREY J. STEINLE, “The Problem Child of World Trade: Reform School for Agriculture”, *Minnesota Journal of Global Trade*, Spring 2005, p. 336.

(i.e flood mitigation and erosion prevention), rural employment, countryside preservation, among others. All these non-trade concerns fall under the concept of “multifunctionality”⁵. Finally, agricultural industries are some of the most organized and conservative political forces, and have strong lobbying power that makes difficult to change the *status quo* of agricultural protection in countries where subsidies have a practice⁶.

On April 14, 1994 the Uruguay Round negotiations culminated with the signing of the “The Final Act Embodying the Results of the Uruguay Round of Multilateral Negotiations.” This Final Act created the World Trade Organization (WTO), which comprises a list of about 60 agreements, annexes, decisions and understandings⁷. One of these agreements was the AoA, a sectoral agreement negotiated separately from the Subsidies and Countervailing Measures Agreement with its own object and purpose, tailor-made to the particular conditions of agricultural products⁸.

As mentioned before, the AoA was thought with the aim of establishing a fair and market-oriented agricultural trade policy. For purposes of reaching this objective, Members made commitments in the areas of market access, domestic support and export subsidies. In the area of market access, three types of measures were implemented. The first one is the so-called “tarification”, which

5 RAJ BHALA, *Internacional Trade Law: Theory and Practice*, Second Edition, Lexis Publishing, 2001, p. 721-723.

6 JEFFREY J. STEINLE, “The Problem Child of World Trade: Reform School for Agriculture”, *Minnesota Journal of Global Trade*, Spring 2005, p. 337; MELAKU GEBOYE DESTA, “The Bumpy Ride Towards the Establishment of a “Fair and Market Oriented Agricultural Trading System” at the WTO: Reflections Following the Cancun Setback”, *Drake Journal of Agricultural Law*, Fall 2003, p. 493.

7 World Trade Organization, *Understanding the WTO*, http://www.wto.org/english/thewto_e/whatis_e/tif_e/agrm1_e.htm

8 DIDIER CHAMBOVEY “How the Expiry of the Peace Clause (Article 13 of the WTO Agreement on Agriculture) Might Alter Disciplines on Agricultural Subsidies in the WTO Framework”, *Journal of World Trade*, 2002, pp. 310-311.

replaces non-tariff border measures with equivalent tariffs. The second measure is the creation of minimum access tariff-rate quotas, and finally WTO Members scheduled commitments on tariff reductions⁹.

On the other hand, agriculture is the only sector where export subsidies are legal, although, they are subject to reduction commitments on the basis of quantity commitment levels and budgetary outlays¹⁰. Finally, on the domestic support scenario, the AoA makes a distinction between subsidies with trade distorting effects subject to reduction commitments (or Amber Box subsidies), Green Box subsidies, which are payments with minimal trade distorting effects and therefore are excluded from reduction commitments, and payments under production limiting programmes (known as Blue Box subsidies), which are also excluded from reduction commitments¹¹.

This article will only focus on those commitments made by members in the areas of domestic support and export subsidies, and on how AoA provisions on this matter could be used by countries to erode the purpose of creating a fair and market oriented agricultural trade policy.

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- 9 RAJ BHALA, "World Agricultural Trade in Purgatory: The Uruguay Round Agriculture Agreement and its Implications for the Doha Round", *North Dakota Law Review*, 2003, p. 714.
 - 10 MELAKU GEBOYE DESTA, "The Bumpy Ride Towards the Establishment of a "Fair and Market Oriented Agricultural Trading System" at the WTO: Reflections Following the Cancun Setback", *Drake Journal of Agricultural Law*, Fall 2003, p. 515.
 - 11 RAJ BHALA, *Internacional Trade Law: Theory and Practice*, Second Edition, Lexis Publishing, 2001, p. 687.

III. THREE PROBLEMS OF THE AGREEMENT ON AGRICULTURE WITH RESPECT TO SUBSIDIES

1. THE POSSIBILITY TO CHALLENGE AGRICULTURAL EXPORT SUBSIDIES UNDER SCM AGREEMENT PROVISIONS.

Since the “Peace Clause” expired¹² there have been different opinions when it comes to determine the future application of the Subsidies and Countervailing Measures Agreement (hereinafter SCM) provisions to agricultural export subsidies¹³. The issue raises a very important question since, depending on the answer, WTO Members could be either challenged under SCM provisions when their measures cause adverse effects to the interests of other Members, or protected from the application of SCM rules even if their measures cause adverse effects to the interests of other Members.

Within the frame of the WTO, Agreements generally apply cumulatively¹⁴. This implies that if there are no contradictions between provisions of two WTO Agreements (case in which the provisions of the more specific Agreement would prevail), the rules of these two Agreements would apply at the same time when resolving a particular case.

12 The Peace Clause was a provision that excepted, among other things, agricultural export subsidies from being challenged under the SCM Agreement if they caused adverse effects to the interests of another Member. See, Agreement on Agriculture of 15 April 1994, LT/UR/A-1/2, Article 13.

13 RICHARD H. STEIMBERG and TIMOTHY E. GOSLING, “When the Peace Ends: The Vulnerability of EC and US Agricultural Subsidies to WTO Legal Challenges”, *Journal of International Economic Law*, 2003; DIDIER CHAMBOVEY, “How the Expiry of the Peace Clause (Article 13 of the WTO Agreement on Agriculture) Might Alter Disciplines on Agricultural Subsidies in the WTO Framework”, *Journal of World Trade*, 2002.

14 Report of the Panel, *United States Subsidies on Upland Cotton*, WT/DS267/R, 8 September 2004, para 71.071. Another cases analysing the relationship between the GATT and the other Annex 1^a Agreements, see Report of the Panel, *Brazil-Measures Affecting Desiccated Coconut*, WT/DS22/R, 17 October 1996, para. 227, recalled in the Appellate Body Report, *Argentina- Safeguards Measures on Imports of Footwear*, WT/DS121/AB/R, 14 December 1999, paras 79- 81.

To some Scholars, since the Peace Clause expired, no exception or contradiction exists between SCM “actionable subsidies provisions” and the AoA and therefore, the door is opened for members to bring claims under the SCM against agricultural subsidies if they cause adverse effects to the interests of other members. To other Scholars¹⁵, however, the application of the SCM to agricultural export subsidies is not that obvious. For them the fact that the AoA has specific provisions dealing with agricultural export subsidies is determinative when analyzing the problem.

The general rule established in the SCM Agreement is that all types of export subsidies are prohibited. Although, the AoA has an exception that allows Members to grant export subsidies if they are in compliance with reduction commitments levels¹⁶. This exception could be used to argue a contradiction between export subsidy provisions between the AoA and the SCM. However, the most important argument to assert that Members cannot be challenged under SCM provisions, if they comply with AoA export subsidy provisions, is the fact that every export subsidy causes trade-distorting effects. Accordingly, if this is the result of this type of support, every export subsidy granted by a government would cause adverse effects to the interests of another member, and therefore, every export subsidy would violate Part III of the SCM Agreement. If this is true, there is no explanation to why did Members allow the granting of agricultural export subsidies in Article 8 of the AoA, if afterwards these payments were to be challenged under Part III of the SCM because of adverse effects.

Arguments concerning the application of the SCM Agreement and the possible challenge of agricultural export subsidies under SCM provisions are available for challenging countries and for

15 DIDIER CHAMBOVEY, “How the Expiry of the Peace Clause (Article 13 of the WTO Agreement on Agriculture) Might Alter Disciplines on Agricultural Subsidies in the WTO Framework”, *Journal of World Trade*, 2002, pp. 305-352.

16 Agreement on Agriculture of 15 April 1994, LT/UR/A-1^o/2, Article 8. Agreement on Subsidies and Countervailing Measures of 15 April 1994, LT/UR/A-1A/9. Part II.

defending countries. However, legal interpretations cannot serve as a mean to justify agricultural trade-distorting effects that do not correspond with the purpose of the AoA: to create a fair and market oriented Agricultural trade policy.

2. HIDING EXPORT SUBSIDIES BEHIND DOMESTIC SUPPORT MEASURES

One of the deficiencies of the AoA on which Scholars agree is the lack of prohibition of indirect practices that are not contingent on export but are capable of promoting exports. The latter allows Members to disguise a subsidy deemed to have effects on the foreign market by providing it irrespective of export performance considerations¹⁷.

According to Article 1(e) of the AoA, an export subsidy is a payment contingent upon export performance. On the other hand, this Agreement does not define what a domestic support is, but it can be understood as a payment provided to agricultural producers regardless of whether the products are exported or not¹⁸.

As it was previously mentioned, the AoA establishes reduction commitments to domestic support (amber box) and export subsidies. However, the undertakings on domestic support reductions are more permissive than those on export subsidies. The first difference is that

17 GONZÁLEZ CARMEN G., "Institutionalizing Inequality: the WTO Agreement on Agriculture, Food Security, and Developing Countries", *Columbia Journal of Environmental Law*, 2002, paras. 465 and 487, quoting Ian Sturgess. The Liberalisation Process in International Agricultural Trade: Market Access and Export Subsidies, in *Negotiating the Future of Agricultural Policies: Agricultural Trade and the Millennium WTO Round*. SANOUSSI BILAL & PAVLOS PEZAROS eds., 2000, p. 150; WILLIAM PETIT. The Free Trade Area of the Americas: Is It Setting the Stage For Significant Change In U.S Agricultural Subsidy Use?, *Texas Tech Law Review*. para. 143, quoting MELAKU GEBOYE DESTA. *The Law of International Trade in Agricultural Products*, s.e., 2002, p. 177.

18 MELAKU GEBOYE DESTA, "The Bumpy Ride Towards the Establishment of "a Fair and Market Oriented Agricultural Trading System" at the WTO: Reflections Following the Cancun Setback", *Drake Journal of Agricultural Law*, Fall 2003, p. 521.

commitments to reduce domestic support measures (i.e amber box) apply at sector level rather than at product level, as it occurs in export subsidies reduction commitments. This situation, allows countries to legally increase product-specific amber-box support at any level if they do not exceed the corresponding annual or final bound commitment level specified in its Schedule¹⁹, contrary to what occurs in export subsidies reduction commitments where such a flexibility is not possible²⁰.

Furthermore, the AoA establishes higher reduction levels on export subsidies than on domestic support payments. Hence, the AoA demands from the Member a 36% reduction on budgetary outlays (24% for developing countries) and of 21% on quantities of subsidized exports (14% for developing countries), as compared with the reduction commitments required to domestic support: 20% for developed countries and 13% for developing countries.

For this reasons, WTO Members find more attractive to promote exports either by granting subsidies without export contingency or by granting domestic support and export subsidies at the same time. This situation erodes the purpose of the AoA to create a distinction between the domestic support and the export subsidies disciplines, affecting directly the goal to achieve the liberalization of the export market in a phasing out process²¹.

19 MELAKU GEBOYE DESTA, "The Bumpy Ride Towards the Establishment of "a Fair and Market Oriented Agricultural Trading System" at the WTO: Reflections Following the Cancun Setback", *Drake Journal of Agricultural Law*, Fall 2003, p. 525.

20 Modalities for the Establishment of Specific Binding Commitments, Note by the Chairman of the Market Access Group, MTN.GNG/MA/W/24, 20 December 1993.

21 WTO, Doha Ministerial Declaration, WT/MIN(01)/DEC/1, 20 November 2001, Work Programme - Agriculture.

3. BLUE BOX SUBSIDIES MAY HAVE MORE TRADE DISTORTING EFFECTS THAN AMBER BOX SUBSIDIES

Direct payments under production limiting programmes are excluded from domestic support reduction commitments. Consequently, there are subsidies not subject to WTO control which may cause trade distorting effects in the Agricultural market.

Under the AoA, direct payments made to farmers under production-limiting programmes (i.e Blue Box measures) are excluded from the reduction requirements on the condition that two elements are satisfied. First of all, the payments need to be “direct” payments; second, payments should be conditional upon some form of production-limiting measures being taken by the recipient, including on a fixed acreage and yields, or on eighty-five percent or less of the base level production, or, in the case of livestock payments, on a fixed number of head²².

The problem arises when trade-distorting effects appear as a consequence of granting legal blue box subsidies. According to the AoA, there are three categories of domestic support: Green box subsidies with no or at most minimal trade-distorting effects²³; Amber box measures with significant -or more than minimal trade-distorting effects²⁴; and Blue box measures which are defended on the economic ground that production limiting programmers are less trade-distorting than Amber Box²⁵. However, there is no clear

22 MELAKU GEBOYE DESTA, “The Bumpy Ride Towards the Establishment of “a Fair and Market Oriented Agricultural Trading System” at the WTO: Reflections Following the Cancun Setback”, *Drake Journal of Agricultural Law*, Fall 2003, p. 531; Agreement on Agriculture of 15 April 1994, LT/UR/A-1/2, Article 6.5.

23 Agreement on Agriculture of 15 April 1994, LT/UR/A-1/2, Annex II.

24 MELAKU GEBOYE DESTA, “The Bumpy Ride Towards the Establishment of “a Fair and Market Oriented Agricultural Trading System” at the WTO: Reflections Following the Cancun Setback”, *Drake Journal of Agricultural Law*, Fall 2003, p. 524; Agreement on Agriculture of 15 April 1994, LT/UR/A-1/2, Article 6.1.

25 RAJ BHALA, “World Agricultural Trade in Purgatory: The Uruguay Round Agriculture Agreement and its Implications for the Doha Round”, *North Dakota Law Review*, 2003, p. 794.

standard within the AoA or any other treaty which establishes what kind of effects should these payments have. Accordingly, these subsidies are not subject to reduction commitments and there is no way to control their effects within WTO law. Members that take into place production limiting programmes are able to provide unlimited amounts of payments disregarding the possible effects of these payments.

It must be mentioned that the amount of the payments granted within blue box programs is not limited. It is also important to address the fact that these payments are not conditioned to production-limiting, therefore these can be decoupled from production. These doubts surrounding the Blue Box subsidies illustrate the necessity to regulate this instrument in particular so that it can stop serving as a trade distorting element.

The situation mentioned above, impedes the goal of the WTO to move towards substantial reductions in trade-distorting domestic support as established by the Doha Round Declaration²⁶.

26 WTO, Doha Ministerial Declaration, WT/MIN(01)/DEC/1, 20 November 2001, Work Programme - Agriculture.

IV. CLAIMANT'S WRITTEN SUBMISSION

On Submission to the Panel of the World Trade Organization
At The Centre William Rappard
Geneva, Switzerland

Elsa Moot Court Competition on wto Law 2005/2006
Dispute

Subsidia – Agricultural Subsidies on Sweet Biscuits, Wheat & Pork
Competia Vs. Subsidia
Submission of the Complainant Competia
January 2006

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34. Modalities for the Establishment of Specific Binding Commitments, Note by the Chairman of the Market Access Group, MTN.GNG/MA/W/24, 20 December 1993.
35. European Communities, *Common Organization of the Market in Wine*. Council Regulation (EC) No. 1493/1999 of 17 May 1999.

List of Abbreviations

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| AB | Appellate Body |
| AoA | Agreement on Agriculture |
| DSU | Dispute Settlement Understanding |
| GATT | General Agreement on Tariffs and Trade |
| PC | Peace Clause |
| PS | Pork Scheme |
| SB | Sweet Biscuits |
| SBM | Sweet Biscuits Manufacturers |
| SBS | Sweet Biscuits Scheme |

| | |
|-----|--|
| SCM | Agreement on Subsidies and Countervailing Measures |
| WP | Wheat Producers |
| WTO | World Trade Organization |
| WTO | Agreement Marrakech Agreement Establishing the |
| WTO | |

STATEMENT OF THE FACTS

Subsidia is a developed WTO Member, which has a long-standing tradition of subsidizing its farmers and agribusiness interests. *Competia* is a developing WTO Member that has been affected due to *Subsidia*'s policies on agricultural subsidies. *Competia* formally requested the formation of a panel after consultations in order to address the subsidies in three different products: SB, wheat and pork.

Regarding SB, since its raw material is produced at expensive prices in *Subsidia*, the government subsidizes all SB if they produce with domestic ingredients. These overly generous payments are bringing the prices too far down, allowing manufacturers to sell their product 10-15% below the average total cost of production and 5-10% below world market prices. Furthermore, *Subsidia* has scheduled its export subsidy commitments on SB as follows: 55 million subs and 600.000 tonnes. Since 90% of the exported SB are subsidised, *Subsidia* is exceeding its quantity commitments.

Moreover, *Subsidia* grants price contingent export subsidies to its WP within its budgetary commitments in order to ensure they will not be affected by fluctuations in the world market price and demand. These payments have been granted the last ten years, allowing *Subsidia*'s share of the world market to grow steadily 5% each year. Since year 2002, this country has been gaining two per cent of the total share of the wheat world market. Nowadays, *Subsidia* has 39% of the share on the wheat world market.

Finally, *Subsidia* is the current leading exporter of pork. Econometric models demonstrate that this will be the case in year 2015 unless the world market changes dramatically. *Subsidia* provides to its farmers a domestic support scheduled as a Blue Box –Article 6.5 (a) (iii)- in order to limit the production from 9 million to 7 million swine. Exports in the year 2004 amounted to the equivalent of 7 million swine, at prices 15% below the average cost of production and 20% below world market prices. Farmers receive the same amount of subsidies each year provided that they cut production according to a plan laid out for each farm. If a farmer exceeds the number of heads in

a given year, he loses 50% of his support payments that year and for the next year as well.

Summary of Claims-Identification of Obligations and Breaches

Regarding Wheat

Claim 1: Since the Peace Clause expired, restrictions regarding the application of Part III of the Agreement on Subsidies and Countervailing Measures to agricultural subsidies are no longer in place. Thus, since the SCM and the Agreement on Agriculture shall apply cumulatively, agricultural payments can be challenged under Articles 5 and 6.3 of the SCM if they cause adverse effects to the interest of other Members.

Claim 2: The fact that a country is granting an agricultural export subsidy within its scheduled commitments does not mean that such payment is non-actionable. Article 8 of the AoA only makes this type of payments legal, but it does not exempt those agricultural subsidies from being actionable under part III of the SCM.

Claim 3: Paragraph 6.3 (d) of the SCM applies to agricultural products because footnote seventeen of that Agreement does not inhibit the application of that paragraph to the agricultural sector as such, but only to particular products with multilaterally agreed specific rules.

Claim 4: Proving occurrence of one of the situations described in Article 6.3 of the SCM suffices to conclude that serious prejudice in the sense of Article 5 (c) has arisen. This has its basis, *inter alia*, on the fact that there are no other express requirements guiding the proof of serious prejudice within the WTO Agreements or Rulings.

Claim 5: Subsidia's price-contingent export subsidies cause serious prejudice to the interests of Competia, since the effect of the payment is an increase in Subsidia's wheat world market share in the sense of Article 6.3 (d), due to an overproduction of wheat created by Subsidia that was sold overseas.

Claim 6: Subsidia's payments cause serious prejudice to the interest of other Members since they cause a significant price depression of world market prices, as they allow producers to sell the product in foreign markets at prices lower than the ones prevailing in the world market.

Regarding the SBS

Claim 1: Since Subsidia is exporting SB in quantities beyond its schedule commitments, it has the burden of proving that it did not subsidised the exceeded quantity of exports in question, regarding Article 10.3 of the AoA.

Claim 2: Nonetheless Subsidia has the burden of proving that it is not granting subsidies in excess of its schedule commitments, Competia will draw the attention of the panel to the dispute before it. In this way, Subsidia is granting generous subsidies that created a “spill over” unlimited support on the export market for SB manufactures, constituting a subsidy under Article 9.1 (c) of the AoA. As Subsidia is providing these subsidies beyond its schedule commitments, its payments are in contravention of Articles 3.3 and 8 of the AoA.

Regarding the PS

Claim 1: Subsidia’s payments to pork producers do not constitute Blue Box domestic support measures, since a percentage of the payment is decoupled from production. The fact that a producer will receive 50% of the payment regardless of whether it limits production or not shows that the subsidy is not a Blue Box measure. This violates articles 6.5 (a), 3.2, 6.1 and 6.3 of the AoA.

Claim 2: Subsidia’s measure is a domestic support that creates a “spill over” on the exports, constituting in this way a subsidy under Article 9.1 (c) of the AoA. Accordingly, Subsidia’s payments are on the export (since they confer an advantage which is reflected in the favourable conditions upon which swine producers can export), and are financed by virtue of governmental action. Since Subsidia should have scheduled these payments, but it did not, this country has acted inconsistently with its obligations under Articles 3.2, 6.1, 6.3, 9.1(c), 3.3 and 8 of the AoA.

Arguments

I. Wheat

1. Application of Article 5 (c), 6.3 (c) and (d) of the SCM to Agricultural Subsidies

Competia will demonstrate that since article 13 of the AoA expired, the SCM and the AoA apply cumulatively when no contradiction exists between

the content of their provisions. Since there is none between Articles 5 (c), 6.3 (c) and (d) of the SCM and the AoA, these provisions apply to agricultural subsidies.

1.1. Application of the SCM Agreement to an Agricultural Subsidy- PC Ends

Competia will demonstrate that after the PC¹ agricultural subsidies are not exempt from actions under part III of the SCM. Therefore, since there is no contradiction between the AoA and the SCM, this type of subsidies can be challenged if they cause *serious prejudice* to the interests of another Member.

In agricultural issues, Article 21.1 of the AoA states that provisions of GATT 1994 and other Multilateral Trade Agreements contained in Annex 1A to the WTO Agreement [SCM] shall apply *subject to the AoA rules*. Taking this into account, WTO rulings² and scholars³ have agreed in the application of the SCM and the AoA Agreements, concluding that these apply cumulatively and that, provisions of the AoA shall prevail only in case of conflict between them. Accordingly, article 5 (c), and Paragraphs 6.3 (c) and (d) shall apply to agricultural export subsidies unless there is a contradiction between them and the AoA. Before January 1, 2004, Article 13 (c) (ii) of the AoA exempted agricultural export subsidies from actions based on article XVI of GATT 1994 and articles 3, 5 and 6 of the SCM. Nowadays, that this provision has

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- 1 Article 13 (“due restraint”) of the AoA protected countries that used export subsidies only to the extent permitted by the Agreement from being challenged under Article 3, 5 and 6 of the SCM Agreement. See, Agreement on Agriculture of 15 April 1994, LT/UR/A-1A/2, Article
 - 2 Report of the Panel, United States Subsidies on Upland Cotton, WT/DS267/R, 8 September 2004, para 71.071. Another cases analysing the relationship between the GATT and the other Annex 1A Agreements, see Report of the Panel, Brazil-Measures Affecting Desiccated Coconut, WT/DS22/R, 17 October 1996, para. 227, recalled in the Appellate Body Report, Argentina-Safeguards Measures on Imports of Footwear, WT/DS121/AB/R, 14 December 1999, paras 79-81.
 - 3 Didier Chambovey, “How the Expiry of the Peace Clause (Article 13 of the WTO Agreement on Agriculture) Might Alter Disciplines on Agricultural Subsidies in the WTO Framework”, *Journal of World Trade*, 36(2) (2002), 305-352 (pp. 308-309). Richard H. Steimberg and Timothy E. Fosling, “When the Peace Ends: The Vulnerability of EC and US Agricultural Subsidies to WTO Legal Challenges”, *Journal of International Economic Law*, 6 (2) (2003), 369-417 (pp.374-375).

already expired⁴ there is no restriction to present a claim under articles 3, 5 and 6 of the SCM against agricultural subsidies.

An additional argument support the application of Articles 5 and 6 of the SCM to agricultural subsidies since the expiration of the PC. The inception of Article 13 in the AoA demonstrated that Members believed that, in the absence of this article, claims under part III of the SCM would be allowed against agricultural subsidies⁵. To sum up, since the expiry of the PC, those restrictions regarding the SCM application are no longer in place. Hence, since these Articles are not in contradiction, they indeed apply to agricultural export subsidies.

1.2 Application of Article 5 (c), and Article 6 Paragraphs (c) and (d) of the SCM

Having illustrated that the SCM Agreement applies to agricultural subsidies, Competia will demonstrate that every export subsidy that causes serious prejudice to the interests of another member may be challenged under part III of the SCM, regardless of whether the subsidy complies with the scheduled commitments or not. Article 8 of the AoA states that each WTO Member undertakes not to provide export subsidies other than in conformity with that Agreement and with the commitments as specified in each Member's Schedule⁶. This Article constitutes an exception to the general prohibition in part II of SCM that compels Members not to grant export subsidies except as provided under the AoA. Regarding the latter, Article 8 of the AoA makes every export subsidy that conforms that with agreement and the notified commitments legal. However, the fact that a subsidy is legal does not mean that it is not actionable. Article 8 of the AoA only exempts agricultural subsidies from being illegal, but it does not exempt them from being actionable –something the PC did before its expiration–⁷. Thus, compliance with the AoA and its scheduled commitments does not shelter agricultural

4 The chapeau of Article 13 of the AoA states that its provisions would be applicable during the implementation period. Since article 1 paragraph f) of the same agreement states that the implementation period for article 13 is 9 years beginning in 1995, the Peace clause expired in December 31, 2003. Agreement on Agriculture, Article 13.

5 David Morgan and Goh Gavin, "Peace in Our Time, An Analysis of Article 13 of the Agreement on Agriculture", *Journal of World Trade*, 37(5) (2003), 997-992 (p.986).

6 Agreement on Agriculture, Article 8.

7 Didier Chambovey, "How the Expiry of the Peace Clause...", p. 323. See also, Richard H. Steimberg and Timothy E. Fosling, "When the Peace Ends", p. 377.

subsidies from claims under part III –Article 5- of the SCM Agreement. Accordingly, actionable subsidies are not prohibited, but can be challenged before the WTO when they cause adverse effects through serious prejudice to the interests of another Member⁸.

1.3 How does Article 6.3 (d) apply to agricultural subsidies?

Now that Competia has already proven that part III of the SCM applies to agricultural subsidies and that, the fact that a Member complies with its export subsidies reduction commitments does not mean that these subsidies are not actionable, it will prove how agricultural subsidies can be challenged under Article 6.3 (d) of the SCM regardless the existence of footnote 17 in that provision.

Article 6.3 (d) of the SCM provides an exception to its application through footnote 17 therein. Accordingly, the serious prejudice will rise in the sense of this Article “*unless other multilaterally agreed specific rules apply to the trade in the product or commodity in question*”⁹.

The US-Cotton Panel and the AB have accepted the application of subparagraph (d) to agricultural subsidies, and therefore, have acknowledged that footnote seventeen applies only to particular products and not to the whole agricultural sector as such¹⁰.

Even though in the US-Cotton case neither the Panel nor the AB found that there had been a violation of subparagraph 6.3(d), and therefore of Article 5(c) of the SCM Agreement, this was not because they considered that the provision did not apply to agricultural subsidies but rather that the claimant was unable to present a *prima facie* case¹¹. Hence, through its analysis neither the Panel nor the AB¹² excluded the application of this provision to agricultural subsidies¹³.

8 Ibidem.

9 Agreement on Subsidies and Countervailing Measures, Footnote 17.

10 See, Report of the Panel, US-Cotton, para. 7.1389; Appellate Body Report, United States - Subsidies on Upland Cotton, WT/DS267/AB/R, 3 March 2005, paras. 505-513.

11 Report of the Panel, US-Cotton, para. 7.1464.

12 Appellate Body Report, US-Cotton, paras. 497-512.

13 Report of the Panel, US-Cotton, paras. 7,1416-7.1464.

Furthermore, from the text of the Article 6.3 (d) it can be noted that footnote 17 is a reference to multilateral agreements on specific commodities such as *The Dairy Agreement* and *The International Bovine Meat Agreement*, and does not preclude the application of subparagraph 6.3(d) of the SCM to other agricultural products that do not have particular agreements –such as wheat-. This interpretation has its basis on the particular words used in subparagraph (d) and its footnote 17 as they refer to “the product or commodity” in singular and not to a sector of products as it would be the agricultural sector¹⁴.

Therefore, it has been established how Article 6.3 (d) applies to agricultural products unless there is a multilateral agreement on a specific commodity, which is not the case of wheat.

The above-mentioned arguments allow Competia to conclude that Subsidia’s price contingent export subsidies can be challenged under part III of the SCM (including Article 6.3 (d), and that the fact that Subsidia complies with its budgetary commitments does not imply that its payments cannot cause adverse effects to the interests of other Members.

2. Subsidia’s measure violates Article 5(c) of the SCM

Now that Competia has established the application of part III of the SCM to agricultural subsidies, it will demonstrate that Subsidian price-contingent export subsidies are causing serious prejudice to the interests of other Members in the sense of Articles 6.3(c) and (d) of the SCM, violating Article 5(c) of the same Agreement. In order to prove the latter, Competia will first show how proof of one of the situations described in Article 6.3 is sufficient to constitute serious prejudice in the sense of Article 5(c) of the SCM. Afterwards, the claimant will illustrate the way how Subsidian export subsidies fit in two of the situations in Article 6.3 of the SCM, i.e. price depression (6.3(c)) and increase in the world market share (6.3(d)).

2.1. Demonstration of one of the Situations in Article 6.3 of SCM suffices to constitute Serious Prejudice

Competia will demonstrate how the case where a subsidy fits into one of the situations of Article 6.3 of the SCM, suffices to conclude that serious prejudice has arisen in the sense of article 5(c) of the SCM.

14 Richard H. Steimberg and Timothy E. Fosling, “When the Peace Ends”, p. 387.

The SCM Agreement provides a list of situations in which serious prejudice to the interests of another member may arise. In interpreting this provision, the *US-Cotton* Panel stated that whenever it is proven that one of these four situations listed in paragraph 6.3 arises, serious prejudice in the sense of Article 5(c) of the SCM exists. Quoting the Panel:

We therefore do not believe that, once we have concluded that the conditions in Article 6.3(c) are fulfilled, and thus that serious prejudice “in the sense of paragraph (c) of Article 5 “may” arise, a separate examination of the existence of “serious prejudice” under the chapeau of Article 6.3 or Article 5(c) is necessary. Our examination of the text, in its context, indicates to us that the Article 6.3(c) examination is determinative also for a finding of serious prejudice under Article 5(c). *That is, an affirmative conclusion that the effects-based situation in Article 6.3(c) exists is a sufficient basis for an affirmative conclusion that “serious prejudice” exists for the purposes of Article 5(c) of the SCM Agreement.* (emphasis added)¹⁵.

Even though in this case the Panel only analysed one of the items of Article 6.3 –item 6.3 (c)-, it shall be understood from the arguments of the Panel that this conclusion applies to all four situations listed in article 6.3 of the SCM, -including item 6.3 (d)-.

When concluding the above-quoted assertion the US-Cotton Panel stressed several reasons. First, the Panel analysed why the use of the word *may* was not meant to establish that those four situations were one of many requirements in the *chapeau* of article 6.3 of the SCM necessary to prove the existence of serious prejudice. Instead, it was intended to show that the list of situations therein was illustrative and not exhaustive¹⁶. Moreover, the Panel identified how Articles 5 and 6 of the SCM have no additional criteria that would guide the interpreter’s examination as to when serious prejudice would or would not arise within the meaning of Article 5(c) once one of the situations described in article 6.3 are fulfilled.

15 Report of the Panel, *US-Cotton*. para 7.1389.

16 “In this respect, we understand that the term “may” was, at least originally, intended to demonstrate that the list in Article 6.3 is illustrative and not exhaustive”, Report of the Panel, *US-Cotton*, para. 7.1387.

This relatively express guidance about certain aspects of Article 6.3 led the Panel to conclude that the situations addressed in that provision are the only conditions in order to find that serious prejudice has arisen in the sense of Article 5(c)¹⁷. Accepting a different interpretation would result in reducing articles 5(c) and 6.3 of the SCM to redundancy or uselessness¹⁸ since the term “serious prejudice” is broad and undetermined, and thus, it would always need express requirements –like the ones in article 6.3- in order to arise.

Furthermore, the Panel also referred to article 6.2 of the SCM for the purposes of interpreting article 6.3, and observed how this provision states that serious prejudice would not be deemed to exist when the subsidising member shows that the subsidy in question has not resulted in any of the situations of paragraph 6.3. The Panel eventually concluded that a symmetrical reading of article 6.2 would be that it identifies the situations listed in Article 6.3 as constituting serious prejudice¹⁹.

The above-mentioned arguments allow Competia to conclude that it is only necessary to prove the existence of one of the situations described in Article 6.3 in order to demonstrate serious prejudice according to Article 5 (c) of the SCM.

2.2. The effects of Subsidia’s export subsidy fit within the situations described in Article 6.3(d) and (c) of the SCM

Regarding what has been stated above, Competia will analyse the way in which the export subsidy provided by Subsidia works, and will conclude that its effects fall in the situations described in Article 6.3(d) and (c) of the SCM, violating Article 5(c) of the same Agreement.

17 Report of the Panel, US-Cotton. para 7.1373.

18 Appellate Body Report, Argentina - Safeguard Measures on Imports of Footwear, WT/DS121/AB/R, 12 december 1999, paras. 82-88. Appellate Body Report, Korea-Definitive Safeguard Measure on Imports of Certain Dairy Products, WT/DS98/AB/R, 14 december 1999, para. 81.

19 Report of the Panel, US-Cotton, Para 7.1380. Some scholars have also agreed with the Panel’s interpretation of article 6.3 of the SCM Agreement. Richard H. Steimberg and Timothy E. Fosling, “When the Peace Ends”, p. 385.

2.2.1. How does the Subsidian Export Subsidies Scheme Works

In order to prove the violation of Subsidia of the SCM, first, it is necessary to understand the architecture of the defendant's measure by explaining the way in which the price-contingent subsidy works, as well as the effects it has over prices, production and exports.

The main element of a price-contingent subsidy is that the amount payable to the recipient is directly linked to a variable price (which is usually the world market price)²⁰. Accordingly, Governments establish a fixed price and a variable price that work in a way in which the difference between them will constitute the amount payable to the recipient²¹. From the facts of this case it can be noted that the aim of Subsidia's price-contingent export subsidies is to assure that WP are not adversely affected by fluctuations in world market price and demand. In order to achieve this goal, Subsidia has to pay an amount of money whenever the world market price (which is the variable price in this case) is lower than a fixed price established by Subsidia (hereinafter "target price"). This target price, which is the minimum amount Subsidia considers its producer should receive so as not to be affected by fluctuations, would have to be *at least* the cost of production for wheat plus a level of income²². Accordingly, every time the world market price is lower than the target price, Subsidia will pay its WP the difference in order to make them "competitive" again in the world market.

The aftermath of this type of scheme is that Subsidia's Government ensures WP a stable position in the market by *insulating* them from world market fluctuations. As a consequence, wheat production decisions are not made

20 The US-Cotton Panel considered four of the United States payments to be price-contingent subsidies since they were directly linked to World market prices. Report of the Panel, US-Cotton, para 7.1289.

21 This is a common element in the four US subsidies that the US-Cotton Panel considered to be price-contingent export subsidies, i.e. marketing loan programme payments, user marketing (Step 2) payments, counter cyclical payments and MLA payments.

22 A payment equivalent to the cost of production would only allow the recipient to avoid losses. However, only a payment including cost of production plus a level of income would permit producers to invest in the next crop year and therefore, to continue on the market. The latter would be the only way in which producers would not be adversely affected by a negative fluctuation.

in consideration of world market behaviour²³, since producers are protected by a “bullet-proof jacket” against adverse changes in world market prices and demand. The latter will encourage more production by regular producers and make the business attractive to new producers as well, since the risk of the business would be minimal²⁴.

The above-mentioned effect (increment in wheat production) increases the supply of the product in the world market since the subsidy will only be granted if the product is exported. The latter will cause serious prejudice through an increase in the world market share and a world price depression, as it will be demonstrated subsequently.

2.2.2 Subsidia’s increase in the wheat world market share constitutes serious prejudice in the sense of Article 5 (c) and 6.3 (d) of the SCM

In order to demonstrate that Subsidia is causing serious prejudice to the interests of Competia, the claimant will prove how article 6.3 (d) applies to the situation that takes place in this case.

The US Cotton Panel stated that the content of the above-mentioned Article consists of six definitional elements: “(i) *the effect of the subsidy*; (ii) *is an increase in the world market share*; (iii) *of the subsidizing Member*; (iv) *in a particular subsidized primary product or commodity*; (v) *as compared to the average over the preceding period of three years*; and (vi) *this increase “follows a consistent trend over a period when subsidies have been granted”*”²⁵.

23 While analysing a price-contingent subsidy the US-Cotton Panel said: “The further the adjusted world price drops, the greater the extent to which United States upland cotton producers’ revenue is insulated from the decline, numbing United States production decisions from world market signals”. US-Cotton Panel, para. 7.1293.

24 The US-Cotton Report of the Panel analysed the effect of the US Counter Cyclical Payments which design is similar to Subsidia’s payments. Regarding this payment the Panel held that market-price contingency subsidies influence production decisions by reducing the revenue risk associated with price variability. Report of the Panel, US-Cotton, para. 7.1301. See also, Roy J. Ruffin and Paul R. Gregory, *Principles of Economics*, 5th edn (Addison Wesley Longman 2001), p. 340.

25 Report of the Panel, US-Cotton, Para 7.1379.

Accordingly, in order to prove the existence of serious prejudice through Article 6.3 (d), Competia will demonstrate the elements mentioned above making special emphasis on the effects of the subsidy.

(i) “The effect of the subsidy”

As stated above, Subsidia’s price contingent export subsidies generate a surplus of wheat that is supplied to the world market. This surplus has the effect of lowering world market prices²⁶, affecting wheat competitors worldwide. Nevertheless, Subsidian producers are not harmed by the negative fluctuation they have caused because of the payment they are receiving from the Government every time the world market price falls below the target price (cost of production plus a level of income).

Consequently, once Subsidia has affected wheat competitors worldwide with its measures, it will begin to gain the part of the world market that others have lost because they have not been able to produce at the new world market prices or, if being able, the business would not be as attractive for them as it was before. Furthermore, due to the Subsidian measures, other world competitors would not have incentives to continue producing or to produce more efficiently –at a lower price–, since every time the world price falls down Subsidian producers will receive money in order to sell at the new world price.

It must be taken into account that, even though Subsidia has been reducing its export subsidies over the ten-year period in which the subsidy has been in place²⁷, this does not mean that Subsidia’s growth should also diminish. The latter based on the fact that the first years in which the subsidy was in place, it allowed Subsidian producers to achieve a very strong position in the market –because they were selling at prices lower than world market prices–, allowing the country to continue its growth even if the percentage of the payment was reduced. As WP have consolidated their position in the world market, the growth of share therein would be very difficult to control, even if payments were withdrawn. Furthermore, attention should be paid to

26 In the US Cotton case the Panel found that price contingent subsidies stimulate production and exports and result in lower world market prices than would prevail in their absence. Report of the Panel, US-Cotton, para. 7.1290 and 7.1298. In the present case Subsidia has the capacity to influence substantially the wheat World market price since it has more than 35% of the World market for the commodity.

27 Facts of the case, para 10.

the fact that a subsidy may have its adverse effects at the time it is conferred, or in the future²⁸.

For the arguments expressed above, Competia asserts that the effect of Subsidia's price-contingent export subsidies is an increase in Subsidia's world market share.

(ii) increase in the world market share of the subsidising Member in a particular subsidised primary product or commodity as compared to the average share it had during the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted.

From the facts it is clear that Subsidia's share of the world wheat²⁹ market has grown with a consistent trend by about 5% each year throughout the ten years in which Subsidia's price-contingent export subsidies program has been in place³⁰. Particularly, the evidence shows that Subsidia's world market share was 35% in 2002, 37% in 2003 and 39% in 2004, therefore, the world market share of Subsidia has increased steadily for the last three years as required by Article 6.3(d).

The arguments mentioned above demonstrate that Subsidia's measure fits the situation described in article 6.3(d) of the SCM Agreement.

2.2.3 Subsidia's export subsidies constitute serious prejudice in the sense of article 5 (c) and 6.3(c) of the SCM.

In this paragraph, Competia will demonstrate how Subsidia's measure does not only constitute serious prejudice through Article 6.3(d), but also through Article 6.3(c), since its measure establishes a significant price depression in the world market³¹.

28 Report of the Panel, Indonesia - Certain Measures Affecting the Automobile Industry, WT/DS54/R, WT/DS55/R, WT/DS59/R, WT/DS64/R, 2 July 1998, para. 14.206. Subsidies granted under expired measures may have had adverse effects at the time they were in effect, and may still have lasting adverse effects.

29 Wheat was recognized as a primary product in the case French Assistance to Exports of Wheat and Wheat Flour, 21 November 1958, L/924 - 7/S/46.

30 Facts of the Case, para 11.

31 The US-Cotton Panel stressed that a "world market" may be the "same market" for the purposes of a claim of significant price undercutting, suppression or depression under article 6.3 (c). Report of the Panel, US-Cotton, para. 7.1248.

a. Price Depression

WTO rulings have established the meaning of price depression stating that it refers to the situations where prices are pressed down or reduced³².

Scholars have agreed that the effect of an export subsidy provided by a country with a significant world market share in a particular commodity, is that it reduces the price of the exported product in importing countries –and therefore in the world market–³³. Hence, since Subsidia's wheat would be sold at lower prices than other countries' wheat (due to the export subsidy), this will enhance the demand for Subsidia's product, all of which compels other competitors to lower the price they charge for wheat in order to remain competitive³⁴. The latter will result in world price depression³⁵.

The price depression is significant

The Panel in the US Cotton case, while analysing some United States price contingent export subsidies, concluded that those measures constituted a *significant* price suppression because the US exerted a substantial proportionate influence in the world upland cotton market, and a link between the US price-contingent subsidies and the world market price existed. On the other hand, since there is no indication in the SCM about the meaning of the word significant, case law in this matter must be considered.

Given the fact that Competia exerts a substantial proportionate influence in the worldwide wheat market³⁶, and its price-contingent export subsidies are directly linked to wheat world market prices (insulating Subsidian producers from low prices), there is sufficient basis to conclude that a casual

32 Report of the Panel, US-Cotton, 7.1276, upheld by the Appellate Body Report, US-Cotton, paras. 423-424.

33 Paul R. Krugman and Maurice Obstfeld. *International Economics: Theory and Practice*, Spanish versión trans. By Yago Moreno, 5th edn (Addison Wesley 2000) p. 267.

34 This was the case in French Assistance to Exports of Wheat and Wheat Flour, 21 November 1958, L/924 – 7/S/46, paras. 17, 18, 19.

35 The effects of Subsidian export subsidies scheme resembles the effects of United States Step 2 Payments scheme that was analysed by the US-Cotton Panel. See, Report of the Panel, US-Cotton, para 7.1298.

36 From the facts of the case it can be regarded that Subsidia has 35%, percentage that is sufficient to exert a big influence in world prices. Facts, para 10.

link exists between the price contingent subsidies and the *significant* price suppression³⁷. Moreover, the increasing percentage in the US market share of wheat as a consequence of the subsidies (5% each year during 10 years) shows that depression of world market prices must be significant in order to reach this amount, all of which affects Competia's wheat produces significantly³⁸.

To sum up, the effect of Subsidia's subsidies is a significant price depression in the world market for the wheat commodity in the sense of Article 6.5 (c) of the SCM.

3. Petition of Remedy

Having demonstrated that (i) the SCM with its articles 6.3 (d) and (c) apply to agricultural subsidies; that (ii) proving one of the paragraphs in article 6.3 suffices to constitute serious prejudice under article 5 (c) of the SCM; and that (iii) Subsidia's measure fits in the situations described in articles 6.3 (d) and (c), Competia requests the Panel to rule that Subsidia brings its measure into compliance with the SCM Agreement since it causes serious prejudice to the interests of Competia in the sense of article 5 (c) of the SCM.

II. *Sweet Biscuits Scheme*

1. Legal Arguments

In the following sections Competia will prove that Subsidia is providing export subsidies listed in Article 9.1 of the AoA to its SB manufacturers. These subsidies are granted beyond the scheduled quantity commitments in violation of articles 3.3 and 8 of the AoA.

1.1 Shift of the Burden of Proof under Article 10.3 of the AoA

According to article 10.3 of the AoA, Subsidia has the burden of proving its compliance with the export reduction commitments within the WTO because

37 Report of the Panel, US-Cotton, par. 7.1347-7.1355.

38 "Although the term 'significant' is not defined, the inclusion of this qualifier in Article 6.3(c) presumably was intended to ensure that margins of undercutting so small that they could not meaningfully affect suppliers of the imported product whose price was being undercut are not considered to give rise to serious prejudice." Report of the Panel, Indonesia-Autos, para 14.254.

it is exporting SB in quantities beyond its scheduled commitments. Article 10.3 provides that “[a]ny Member which claims that any quantity exported in excess of a reduction commitment level is not subsidised must establish that no export subsidy, whether listed in Article 9 or not, has been granted in respect of the quantity of exports in question”.

Article 10.3 has been interpreted consistently by the WTO reports as a shift in the burden of proof, whereby it is up to the claimant to present a *prima facie* case by proving that the responding Member has exported a product in quantities exceeding its scheduled commitments. This article transfers the burden of proof to the respondent, who now has to determine that no export subsidy has been granted in excess of these commitments³⁹.

According to the facts of the case, Subsidia’s commitments are scheduled as 55 million subs and 600.000 tonnes of SB⁴⁰. 60% of the SB production of Subsidia is exported, and 90% of these exports are subsidised, percentage that exceeds the 600,000 Mt commitment independently⁴¹.

Competia has demonstrated that Subsidia is exporting SB in excess of the quantitative commitments what is necessary to shift the burden of proof as per to Article 10.3 of the AoA. Therefore, it will enforce its request by suggesting that the responding Member has granted export subsidies under article 9.1 of the AoA to the quantities exceeding its scheduled commitments. Nevertheless, as explained above, the burden of proof must be shifted to Subsidia. The following sections aim to draw the attention of the Panel to solve the dispute brought before it⁴².

39 Report of the Panel, European Communities - Export Subsidies on Sugar, WT/DS265/R, 15 October 2004, paras. 7.223-7.229; Appellate Body Report, European Communities - Export Subsidies on Sugar, WT/DS265/AB/R, 28 April 2005, para. 249; Report of the Panel, US-Cotton, paras. 7.270-7.273; Appellate Body Report, US-Cotton, paras. 644-645; Appellate Body Report, Canada - Measures Affecting the Importation of Milk and the Exportation of Dairy Products - Second Recourse to Article 21.5 of the DSU, WT/DS103/AB/RW2, WT/DS113/AB/RW2, 20 December 2002, paras. 72 and 74.

40 Facts of the Case, para. 7.

41 Facts of the Case, para. 6 and Clarifications to the Case, question 4.

42 Competia is aware that is the Panel which has the criteria to determine whether the respondent successfully argued to undermine the presumption concerning article

1.2 SBS is a domestic support with unlimited “spill over”

It will be shown that, although the SBS constitutes a subsidy paid without consideration to the export of the product, its “spill over” effect provides unlimited support to exports, undermining the benefits firstly conceded to WTO Members through Subsidia’s export subsidy reduction commitments. Moreover, it will be shown that this “spill over” can be identified as an export subsidy under Article 9.1.c of the AoA, and as it is provided in excess of the quantity commitments, then Subsidia is in contravention of arts. 3.3 and 8 of the AoA.

1.2.1. SBS provides a domestic support

SB scheme provides a domestic support because the payment is granted to all SB producers regardless of whether the product is exported or not⁴³.

According to the facts, “all the SBM get subsidies” if they produce with domestic raw material irrespective of whether the producer sells domestically or for export⁴⁴.

10.3 of the AoA in application of the Principle *Iura Novit Curiae*. See, Appellate Body Report. European Communities - Conditions for the Granting of Tariff Preferences to Developing Countries. WT/DS246/AB/R, on 7 april 2004, para. 105; International Court of Justice, Merits, Case Concerning Military and Paramilitary Activities in and against Nicaragua (Nicaragua v. United States of America), 1986 ICJ Reports, p. 14, para. 29.

- 43 This is what Scholars have understood as domestic support. See, Melaku Geboye Desta. “The Bumpy Ride Towards the Establishment of “a Fair and Market Oriented Agricultural Trading System” at the WTO: Reflections Following the Cancun Setback”. *Drake Journal of Agricultural Law* 8-249 (2003), 489-537 (para. 522); William Petit, “The Free Trade Area of the Americas: Is It Setting The Stage For Significant Change In U.S Agricultural Subsidy Use?”, *Texas Tech Law Review* 37 (2004), 127-166 (para. 137).
- 44 Clarifications to the case, Introduction to SB; facts, para, 5. Consequently, the Us-Cotton Panel assessing the user marketing (Step 2) payments stated that “[w]e are not dealing here, for example, with a subsidy that is paid to a producer irrespective of whether the producer sells domestically or for export. Rather, this measure involves payment to two distinct sets of recipients (exporters or domestic users) in two distinct factual situations (export or domestic use). (emphasis added). Report of the Panel. Us-Cotton, para, 7.732.

Furthermore, the design of the Scheme includes a system that tracks whether the subsidised product is sold in the domestic or export market. Nonetheless, the Scheme only allows Subsidia to determine how to account the subsidy within the schedules, without having any effect on the way the Government grants payment.

The Scheme therefore indicates that the subsidy is a domestic support itself because of the lack of export contingency when the payment is granted.

1.2.2 The “spill over” effect of the domestic support

Subsidia will explain the way in which the AB understood the meaning of the “spill over” as the effect of a domestic support that provides a benefit on exports. One of the commonly understood deficiencies of the AoA⁴⁵ is the lack of prohibition of indirect practices that are not contingent on export but are certainly capable of promoting exports. Such defect allows Members to disguise a subsidy deemed to have effects on the foreign market by providing it irrespective of export performance considerations.

The AB, acknowledging the problem mentioned above, approached the “spill over” issue in the Canada Dairy dispute as follows:

“It is possible that the economic effects of WTO-consistent domestic support in favour of producers may “spill over” to provide certain benefits to export production, especially as many agricultural products result from a single line of production that does not distinguish whether the production is destined for consumption in the domestic or the export market”⁴⁶.

45 Carmen G. Gonzalez, “Institutionalizing Inequality: the WTO Agreement on Agriculture, Food Security, and Developing Countries”, *Columbia Journal of Environmental Law*, 27-433 (2002), 433-490 (paras. 465 and 487); quoting Ian Sturgess, *The Liberalisation Process in International Agricultural Trade: Market Access and Export Subsidies*, in *Negotiating the Future of Agricultural Policies: Agricultural Trade and the Millennium WTO Round*, (Sanoussi Bilal & Pavlos Pezaros eds. 2000) p. 150; William Petit, “The Free Trade Area of the Americas”, p. 143, quoting Melaku Geboye Desta. *The Law of International Trade in Agricultural Products*, s.e. 2002, p. 177.

46 Appellate Body Report, Canada – Dairy (Article 21.5), para. 89.

Subsequently, the AB found a partial solution whilst considering the problem of the “spill over” effect on exports. It established that the objectives intended by the AoA would be undermined when there is no limit to the use of this kind of domestic support. Accordingly, the AB stated that:

“However, we consider that the distinction between the domestic support and export subsidies disciplines in the Agreement *on Agriculture* would also be eroded if a WTO Member were entitled to use domestic support, *without limit*, to provide support for exports of agricultural products. Broadly stated, domestic support provisions of that Agreement, coupled with high levels of tariff protection, allow extensive support to producers, as compared with the limitations imposed through the export subsidies disciplines. Consequently, if domestic support could be used, *without limit*, to provide support for exports, it would undermine the benefits intended to accrue through a WTO Member’s export subsidy commitments”⁴⁷. (emphasis added)

Once the “spill over” effect was explained, Competia will demonstrate in the following subsection that the SBS provides a domestic support with an unlimited “spill over”, in contravention of Subsidia’s benefits conceded under export subsidy commitments.

1.2.3. The subsidy is a domestic support that produces a “spill over”

As explained above, The AB understood the “spill over” as the effect of a domestic support that provides a benefit on exports⁴⁸. Thus, in order to conceptualise the meaning of “spill over”, first of all, we need to have a correct understanding of the terms “benefit” and “on export”.

Regarding the concept of *benefit*, the Panel Report in *Us-Cotton* -based on the SCM- stated that payments confer a benefit when “they place the recipient in a better position than the recipient otherwise would not have been in the marketplace”⁴⁹.

47 Appellate Body Report, *Canada – Dairy* (Article 21.5), para. 91; Appellate Body Report, *EC-Sugar*, para. 280.

48 Appellate Body Report, *Canada – Dairy* (Article 21.5 II), para. 89.

49 Report of the Panel, *Us-Cotton*, para. 7.1116; Report of the Panel, *Canada - Measures Affecting the Export of Civilian Aircraft*, WT/DS70/R, 14 April 1999, para. 7.67.

On the other hand, the term “on export” has been broadly interpreted by the Panel in EC-Sugar, going even beyond the traditional definition of export contingency as follows:

“As discussed before, an analysis of Article 9.1(c) shows that the focus of the analysis is on whether the payment received is “on the export” or *provides an advantage to the exports*, not whether the whole EC regime, or the cross-benefits resulting from A and B quotas are contingent upon C sugar being exported”⁵⁰.

Thus, the facts demonstrate that the main effects of the overly generous subsidies are an advantage to SBM on the export market. The fact that the payments allow sweet biscuit manufacturers to sell its products at prices 10-15% below average cost of production is a proof of the benefit conferred⁵¹. Moreover, the evidence that SBM supply exports at prices 5-10% below world market rates shows that the benefit grants an advantage to the exports⁵². These facts are strengthened by the percentages stating that 90% of the exported SB are produced with subsidised raw material and 60% of the domestic production is being sold in the foreign market⁵³.

As a result, the evidence shows that the SBS places SBM in a better position on the export market than they would have been otherwise. Consequently, the domestic support has an “spill over” effect, as explained in subsection 1.2.2.

1.2.4. Subsidy is a domestic support with unlimited “spill over”

According to the statement of the AB previously quoted (see, footnote 55), the fact that the SBS does not establish any limit to the governmental payments undermines the purpose of the export subsidy commitments.

Two main reasons can be stressed to explain the lack of limit to the “spill over” effect of the domestic support. First, to qualify for the granting of the subsidy the system only requires from the manufacturers the condition to

50 Report of the Panel, EC-Sugar, para. 7.317.

51 Facts of the Case, para. 9.

52 Facts of the Case, para 9.

53 Facts of the Case, para 6.

produce with domestic ingredients⁵⁴. Once this condition is fulfilled by the producer, it does not give any discretionary power to the Government to limit the granting of the payment in consideration to the export commitments⁵⁵.

Second, the scheme created a system that tracks the final destiny of the product in an attempt to comply with the WTO commitments to schedule subsidies in the correct manner. However, this mechanism only affects Subsidia's manner of categorising the respective payment in the domestic or export commitment schedules, without setting a mechanism to limit the granting of the subsidy.

For the reasons stated above, the SBS constitutes a domestic support with an unlimited "spill over" effect that undermines the purpose of Subsidia's reduction commitments.

2. Export subsidies under Article 9.1.c of the AoA

Competia considers that the "spill over" effect of the domestic support is a kind of "payment on the export of an agricultural product financed by virtue of governmental action" that falls under Article 9.1.c of the AoA.

In the EC-Sugar case, the Panel found that a domestic support in the form of minimum price⁵⁶ had a "spill over" effect due to the sale of raw material to sugar exporters at prices below cost of production.⁵⁷ Therefore, the Panel

54 Clarifications to the case, Introduction to SB.

55 In this regard, Competia considers relevant to quote the approach related to the "mandatory/discretionary distinction", acknowledging that "whereby a WTO Member's law as such can be challenged before a WTO panel if the law mandates WTO-inconsistent behaviour. WTO panels have generally found that a law is WTO-inconsistent if they find that it mandates WTO-inconsistent behaviour.⁵⁵ If, on the other hand, the law provides the executive branch of a Member's government with discretionary authority to act in a WTO-consistent manner, then WTO panels have generally found that the law is not WTO-inconsistent". Report of the Panel, *Us-Cotton*, para. 7.401. See also, Report of the Panel, *Canada - Aircraft*, para. 7.56.

56 "Market price support is characteristically provided through insulating domestic markets from the world market. Such insulation is through a combination of barriers to imports, administrative determination of internal supported prices and, where surpluses arise, export subsidies", Raj Bhala. *International Trade Law: Theory and Practice*, 2nd edn (Lexis Publishing 2001), p. 728.

57 Report of the Panel, *EC-Sugar*, para. 7.254-7.293.

ruled that C sugar⁵⁸ producers received payment on export by virtue of governmental action through sales of C beet below the total costs of production to C sugar producers.⁵⁹ Competia considers this finding relevant to this case for two reasons. First, although this is not a case of price support, the direct payment provided to SBM is another form of support system.⁶⁰ Second, both cases are related to the acquisition of raw material by the processor at a discounted price. Furthermore, the requirements to demonstrate the existence of an export subsidy under Article 9.1.c are present in this case. As it was expressed in the Canada Dairy Panel, article 9.1.c demands the demonstration of two elements. Firstly, it requires the presence of payments on the export of an agricultural product, and then, that those payments be “financed by virtue of governmental action”.⁶¹

To begin with, a “payment on exports” appears when the transfer of economic resources allows SBM to acquire raw material below world market prices.⁶² This excess provides Subsidiary producers an advantage to their exports that allows them to sell the final commodity abroad at rates 5-10% cheaper than other world manufacturers. This proves that the “spill over” effect of the SBS constitutes a payment on export as required by Article 9.1.c of the AoA.

In second place, the AB on the Canada-Dairy dispute stated that for a payment to be *by virtue* of governmental action, “there must be a demonstrable link between the *governmental action* at issue and the *financing* of the payments, whereby the payments are in some way financed as a result of, or as a consequence of, the governmental action”⁶³. Considering that in this case Subsidiary’s Government provides a direct monetary contribution to SBM, the payment complies with this requirement.⁶⁴

58 “Sugar produced in excess of A and B quantities, called C sugar, while not subject to quota, is not eligible for domestic price support or direct export subsidies and must be exported”. Report of the Panel, EC-Sugar, para. 3.4

59 Report of the Panel, EC-Sugar, para. 7.293.

60 Raj Bhala. International Trade Law, p. 725.

61 Report of the Panel, Canada-Dairy, para. 7.89.

62 Clarifications to the case, question 5.

63 Appellate Body Report, Canada – Dairy (Article 21.5 II), para. 130; Appellate Body Report, Canada – Dairy (Article 21.5), para. 113.

64 Facts of the Case, para 5.

For the reasons expressed above, Competia considers that the “spill over” effect produced by the SBS is tantamount to an export subsidy under art 9.1.c of the AoA.

2.1 The export subsidy is not contingent on the incorporation of agricultural products in exports

The export subsidies scheduled by Subsidia as “SB” do not constitute a kind of export subsidy described in Article 9.1.f of the AoA, because of the lack of contingency on the incorporation of an exported product upon the granting of the subsidy.

Competia considers that the main element in order to prove the existence of a subsidy under Article 9.1.f is the contingency on the incorporation of an agricultural commodity in the exported product and the granting of the payment, according to the ordinary meaning of the Article.

Regarding the contingency requirement (or second element), The US-Cotton Panel has confirmed that “[t]he meaning of “contingent” is “conditional” or “dependent for its existence upon”.⁶⁵ As explained above, the only requirement that the SBM need to prove for the granting of the subsidy is that they have produced with domestic ingredients. Subsidia argues that it has developed a track system with the objective of identifying the final destination of the product and scheduling the subsidy in the correct manner, however, the track system by itself does not condition the existence of the payment regarding the export, as it is required by the article 9.1.f of the AoA.⁶⁶ Consequently, the contingency on the incorporation of an exported product element is not satisfied by the SBS, which only demands from producers the incorporation in the product independently of its exportation.

65 Report of the Panel, Us-Cotton, para. 7.769.

66 The lack of contingency of the SB Scheme is evident when compared with the export subsidy paid to wine exporters under Article 9.1.f of the AoA. The EC Common Organization of the Market in Wine described on the Council Regulation (EC) n° 1493/1999 of 17 May 1999, requires the presentation of two proofs for the payment of the refund. First, Article 64.2 states that “[t]o qualify for the refund, processed products must, on export, be accompanied by a declaration from the applicant indicating the amounts of raw sugar, white sugar, glucose and glucose syrup used in their manufacture”. Second, the Regulation stipulates that the refund shall be paid on the proof that the products have been exported and have reached the destination mentioned on the export license. In this case, Subsidia shall pay the subsidy just upon the proof of production with domestic raw material.

In addition, if the payment made under SBS was meant to be an export subsidy under article 9.1.f of the AoA, Subsidia would have scheduled its Subsidy as “incorporated products” and not as “Sweet Biscuits”. This is the way Members like the European Communities and Canada have scheduled its subsidies.⁶⁷

Considering the above, Competia concludes that the subsidy under SB Scheme is not an export subsidy under Article 9.1.f of the AoA.

2.2 Obligations upon incorporation of export subsidy commitments on incorporated products

Competia has demonstrated that payments under SB Scheme are not export subsidies on incorporated products. However, if the Panel considers the contrary, Competia alleges that Subsidia still has obligations under budgetary outlays and quantity commitments over the export subsidies provided to SB.

Following the provision stated in Paragraph 9 of Annex 8 to the Modalities Paper,⁶⁸ Members have only scheduled export subsidies under Article 9.1.f of the AoA in terms of budgetary outlays.⁶⁹ However, this is not the case of Subsidia, which has scheduled its export subsidies with two differences. First, it has scheduled commitments as SB and not as incorporated products, and second, it has included reduction commitments on budgetary outlays as well as quantity commitments.

The AB in EC-Sugar has expressed that the Modalities Paper is not an agreement among WTO Members and, by its terms, cannot be the basis of a

67 Facts, para. 6. Regarding Member’s Commitments see, WTO. “Goods Schedules” <http://www.wto.org/english/tratop_e/schedules_e/goods_schedules_e.htm>. [accessed 2 January 2006].

68 “Incorporated Products (...) Base and annual commitment levels shall be established for aggregate budgetary outlays in respect of subsidies on agricultural primary products incorporated in exported products (Annex 7 paragraph 1(f)).” Modalities for the Establishment of Specific Binding Commitments, Note by the Chairman of the Market Access Group, MTN.GNG/MA/W/24, 20 December 1993.

69 See, WTO, http://www.wto.org/english/tratop_e/agric_e/ag_intro04_export_e.htm#reduction [accessed 2 January 2006]; and Europe Communities and Canada Reduction Commitments at WTO, http://www.wto.org/english/tratop_e/schedules_e/goods_schedules_e.htm [accessed 2 January 2006].

dispute settlement under the Marrakesh Agreement.⁷⁰ Furthermore, The AoA establishes in Article 21.2 that “[t]he Annexes to this Agreement are hereby made an integral part of this Agreement”. Thus, the Modalities Paper is a guidance prepared for the negotiators Uruguay Round regarding how to fulfil their reduction commitment obligations, but the binding document is the Schedule of Concessions of the Member annexed to the AoA.⁷¹

Concluding, even if payments to SBM were considered to be export subsidies on incorporated products, Subsidia is obliged to comply with reduction commitments on budgetary outlays and quantities because that was scheduled in its commitments.

3. Violation of articles 3.3 and 8 of the AoA

Competia has established that Subsidia is providing export subsidies listed in Article 9.1 of the AoA to SBM. Additionally, the Claimant demonstrated that Subsidia has export reduction commitments under budgetary outlays as well as quantity commitments. In this section, it will be demonstrated that the Respondent violated articles 3.3 and 8 of the AoA as it provided export subsidies listed in Article 9.1 of the AoA to a commodity in quantities exceeding its commitments.

The Panel in EC-Sugar interpreted Articles 3 and 8 of the AoA harmoniously, establishing that the granting of export subsidies has two limitations. First, export subsidies listed in Article 9.1 of the AoA can only be provided to scheduled products. Second, export subsidies as defined in Article 1(e) of the AoA must not be granted in excess of budgetary outlays and quantity commitment levels.⁷²

Hence, Subsidia has the obligation to provide export subsidies in budgetary outlays and quantity commitment in the levels specified on its Schedule of Concession, as provided in arts. 3.3 and 8 of the AoA. Subsidia’s commitments are scheduled: 55 million subs and 600.000 tonnes SB. 90% of the exported SB are subsidised, and this amount exceeds the 600.000

70 Appellate Body Report, EC-Sugar, para. 199.

71 Raj Bhala. “World Agricultural Trade in Purgatory: The Uruguay Round Agriculture Agreement and its Implications for the Doha Round”, *North Dakota Law Review*, 71-291 (2003), 691-828 (para. 727.).

72 Report of the Panel, EC-Sugar, para. 7.132 and 7.128.

tonnes commitment.⁷³ The latter proves that Subsidia is exporting subsidized quantities beyond its reduction commitments in contravention of arts. 3.3 and 8 of the AoA.

4. Petition of the Remedy

Taking into account all the arguments exposed before, Competia requests the Panel to determine that Subsidia is providing export subsidies listed in Article 9.1 of the AoA in excess of its scheduled commitments thereby contravening Articles 3.3 and 8 of AoA. Therefore, Competia requests the Panel to remedy the situation by asking the responding Member to bring the SB measures into conformity with its obligations under the AoA.

III. Pork Scheme

1. Infringement of Obligations undertaken Pursuant to the Agreement on Agriculture

In this section, Competia will demonstrate that the Pork Scheme violates articles 3.2, 3.3, 6.1, 6.3, 6.5a, 8 and 9.1 of the AoA. Competia will establish that, first, the domestic support regarding this case cannot be considered as a Blue Box measure –violation of article 6.5(a)–. Second, that the measures at hand constitute a domestic support with a “spill over” effect pursuant to article 9.1.c of the AoA –violation of articles 3.2, 6.1, 6.3, 9.1–, and Third, that not scheduling an export subsidy violates articles 3.3 and 8 of the same Agreement.

1.1 The Domestic Support regarding the PS is not a Blue Box Measure

Subsidia argues that the payment granted falls within the description of article 6.5 (a) (iii) of the AoA.⁷⁴ Competia will analyse the context and interpretation governing Article 6.5 a of the same treaty in order to establish that Subsidia’s Pork Scheme violates that provision because the payment is decoupled from production.

73 Facts of the Case, para. 6 and clarifications to the case, question 4.

74 Clarifications to the Case, Introducing the Pork Scheme.

1.1.1 Context and Interpretation Governing Article 6.5.a of the AoA

The establishment of a fair and market oriented agricultural trade policy must condition the interpretation of direct payments under production limiting programmes (Blue box) described in Article 6.5 of the AoA.

Articles 6.5 (a) and (b) of the AoA determine that direct payments under production-limiting programmes are excluded from any Member's calculation of its current total AMS, and thus, from reduction requirements.⁷⁵

The background and conditions described on article 6.5 can be resumed by stating:

“Under the AoA, direct payments made to farmers under production—limiting programs, often known as the “blue box” measures, are excluded from the calculation of the Current Total AMS, and thus, from the reduction requirements on condition that certain important conditions are satisfied. First of all, the payments need to be “direct” payments in the sense that they should not be transferred to farmers through market manipulation devices. Second, payments should be conditional upon some form of production—limiting measures being taken by the recipient, including on a fixed acreage and yields, or on eighty—five percent or less of the base level production, *or, in the case of livestock payments, on a fixed number of heads.*”(emphasis added)⁷⁶

According to the AoA, a blue box measure is in place when the direct payment is conditional to any form of product-limitation program established in Article 6.5(a). However, this is not its only distinction. Hence, Competia will demonstrate that considering the fact that the blue box is excluded from the current total AMS,⁷⁷ the effects of such

75 Agreement on Agriculture, Article 6.5.

76 Melaku Geboye Desta, “The Bumpy Ride...”, p. 531.

77 In order to understand the relevance of the AMS, Scholar Dale Mc. Neil has stated “The calculation of the Total AMS was skewed to allow WTO members to count blue box direct payments to farmers for purposes of the base Total AMS (from which the 20 percent reduction commitment is measured) but to exclude such payments from the calculation of the current Total AMS which is used to determine annual compliance”. Dale Mc. Neil, “Furthering the Reforms of Agricultural Policies in the Millennium Round”. *Minnesota Journal of Global Trade* (2000), 41-86 (p. 58).

subsidies must be less-trade distorting or even benign as some scholars have expressed.⁷⁸

The Vienna Convention establishes that treaties shall be interpreted “in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose”.⁷⁹ Since the objective expressed in the AoA is to establish a fair and market-oriented agricultural trading system⁸⁰, this agreement incorporated reduction commitments on domestic support measures with trade distorting effects such as the ones included in the amber box.⁸¹ Hence, in accordance with the fact that blue box measures were excluded from reduction commitments, these are not supposed to cause the same trade distorting effects such as the ones that are subject to reduction commitments (Amber Box).

Accordingly, in order to determine the consistency of Subsidia’s PS with article 6.5(a) of the AoA, Competia will analyse if the measures are contingent upon a product limitation program, without disregarding the trade distortion caused by the subsidies.

1.1.2 Subsidia’s Pork Scheme

Subsidia’s PS is not a blue box measure since a percentage of the payment is decoupled from production. Accordingly, the facts show that the subsidies are not contingent upon product limitation as Subsidia asserts. Whether the swine production is reduced or not, the producer will receive an

78 Clete D. Johnson, “A Barren Harvest for the Developing World? Presidential “Trade Promotion Authority” and the Unfulfilled Promise of Agriculture Negotiations in the Doha Round”. *The Georgia Journal of International and Comparative Law*, 32 (2004), 437-469 (p. 454).

79 Vienna Convention on the Law of Treaties, Article 31.1; Report of the Panel. *Us-Cotton*, para, 7.965.

80 Agreement on Agriculture. Preamble.

81 According to Raj Bhala “To phrase the definition affirmatively, the Amber Box consists of support payments to farmers or processors that distort trade, production, or prices.” Raj Bhala, “World Agricultural Trade in Purgatory, p. 797.- See William Petit “The AoA considers blue box measures as less trade—distortive and, consequently, subjects them to “production—limiting conditions” that do not need reduction commitments. William Petit, “The Free Trade Area of the Americas”, p. 153.

unconditional 50% of the payment⁸². This situation clearly states that Subsidia has developed a scheme in which half of the direct payment is decoupled from production. Therefore, the PS contradicts article 6.5(a) of the AoA and triggers a series of effects that are clearly trade distorting.

Furthermore, the production limiting programme is intended to reduce the swine production in Subsidia from 9 to 7 million. Subsidia's exports in the year 2004 amounted to the equivalent of 7 million swine⁸³. In 2005, Subsidia remains the leading exporter of pork, and, according to different econometric models, this will be the case in the year 2015. As a result, Subsidia will reduce its amount of swine production by the year 2015 only to the precise amount exported in the year 2004.

In this case, the payment is conditioned upon the number of heads. Therefore, under a complex calculation system, swine production may be reduced, but 50% of the support payment granted under the Blue Box would have no relationship with such an accomplishment. In this context, Subsidia has changed the nature of the Blue Box without affecting its commitments. The PS can be regarded as a measure similar to the EU CAP Reform, which consisted on decoupling direct payments from production. As author Raj Bhala stated:

“In June 2003, the EU heralded the most significant reform to the CAP in a decade, with the EU Agriculture Commissioner, ... To what extent are these changes, which focus on Blue Box payments, helpful in cleansing, and, therefore, in catalyzing the Doha Round talks?... The general reform is to pay farmers directly a flat rate based on historical records, that is, a fixed amount calculated using 2000-2002 as the reference period. This single farm payment will be conditional on farmers adhering to clearly-defined standards for animal and plant health, animal welfare, the environment, food safety, and on cross-compliance (i.e., farmers keeping their land in good agricultural and environmental condition). The idea is to de-couple the single farm payment from production, and thereby ensure farmers will adjust output to market demand signals rather than blithely overproduce”⁸⁴.

82 Facts of the Case, para 13.

83 Facts of the Case, para 14.

84 Raj Bhala, “World Agricultural Trade in Purgatory, p. 799.

The EU performed those measures in order to strengthen its position on the WTO Negotiations by changing the content of the Blue Box. Subsidia however, decided to include decoupled from production payments without changing the nature of subsidies notified under article 6.5 (a) (iii) of the AoA. Furthermore, the payment decoupled from production is allowing farmers to receive an income that is not under the current total AMS, and therefore not subject to reduction requirements. This situation constitutes a violation of articles 6.5 (a) and (b) of the AoA.

Competia has established that the PS is not a Blue Box subsidy. It has stated that there is a 50% payment to the farmers that is decoupled from production, and that the PS grants serious trade distorting effects that allow Subsidia to continue being the first major swine exporter.

1.2 The Nature of the Payment

Competia will establish that the payment is a domestic support with a “spill over” effect that has not been scheduled. This violates Articles 6.1, 6.3 and 3.2 of the AoA. Furthermore, it will consider that the payment is an export subsidy within the terms and conditions described in Article 9.1c of the AoA. Thus, Subsidia acted inconsistently with the content of this article.

1.2.1 Domestic Support and the “spill over” Effect.

As previously stated, the payment in this case is decoupled from production, notwithstanding the provision of articles 6.5 (a) and (b) of the AoA. This income that swine producers receive is a subsidy regardless of whether the products are exported, thus, the 50% that remains constant to the farmer is a domestic support subject to reduction commitments under article 6 of the AoA.

Since the payment is not a blue box measure, it is important to determine what is its nature as a domestic support. The effects of the measure allowed Subsidian exports in year 2004 to be sold 15% below the average cost of production, and 20% below world market prices. These effects are not minimum trade distorting as expressed in the first paragraph of annex II of the AoA. Hence, the payment cannot be considered as a green box measure.

Since the PS is not a blue box or a green box measure, it is considered an amber box measure subject to reduction commitments⁸⁵. Accordingly, since these payments were not subject to such reduction commitments, they are WTO-inconsistent domestic support measures. Therefore, the so called blue box subsidy is nothing but a payment that violates articles 6.1, 6.3 and 3.2 of the AoA.

Regarding the facts, swine production is not conditioned by a process or complex calculation system that determines if the final product is sold overseas or within Subsidia. 7 million swine were exported in the year 2004 from a total amount of production that is not specified, but which cannot overpass the 9 million.

In order to determine if the payment acts solely as a domestic support measure, it is necessary to understand the rationale of the Canada Dairy AB, which stated that the distinction between export subsidies and domestic support measures would be eroded if a member would use domestic support, without limit, to provide support for exports of agricultural products⁸⁶.

In this case, unlike the SBS Scheme, the domestic support measure without limit is granted since the blue box payments are not subject to reduction commitments. Due to the fact that the Blue Box is not conditioned by an amount of money, Subsidia is able to provide support to its swine producers without the obligation to fulfil the requirements of the current total AMS.

Accordingly, since domestic support in this case can be granted without limit, the benefits intended from export subsidy reduction commitments are undermined. Therefore, a “spill over” effect arises⁸⁷. In this case, since swine is not subject to export subsidy reduction commitments, the measure at hand is allowing Subsidia to disregard the purpose and objective of the AoA since the payments are not being included in the current total AMS.

It is clear that a payment decoupled from production, that is granted to every swine producer—regardless of whether it fulfils the product limitation program-, is a domestic support with a “spill over”. Since a large percentage of the swine is being sold overseas, such payment has effects on the export

85 WTO. “Domestic Support in Agriculture”, http://www.wto.org/english/tratop_e/agric_e/agboxes_e.htm, [accessed 4 January 2006].

86 Appellate Body Report, Canada – Dairy (Article 21.5), para 91. See footnote 47.

87 Appellate Body Report, Canada – Dairy (Article 21.5), Para 89. See footnote 48.

market. Accordingly, Competia will analyse if the measures constitute an export subsidy within the meaning of article 9.1 c of the AoA.

1.2.2 Article 9.1.C of the AoA

The 50% payment constitutes an export subsidy under article 9.1 c of the AoA. While analysing the SBS Scheme, Competia explained the requirements in order to constitute a subsidy under article 9.1 c of the AoA⁸⁸. First, a payment on export must exist, and second, it must be financed by virtue of governmental action.

The payment in this case is granted since (1) the swine production can be exported 15% below its total cost of production and (2) 20% under world market prices. From the facts of the case there is a transfer of economic resources. It is now relevant to determine whether that payment constitutes a payment “on export”. Regarding the latter, the EC-Sugar Panel stated:

“An analysis of Article 9.1(c) would put its emphasis on whether the payment in question received is on the export, not on whether, as appears to be the case, the EC price support as a whole is de facto contingent upon C sugar being exported. In other words, when identifying whether a payment is *on the export* as defined under Article 9.1(c) of the *Agreement on Agriculture*, once a payment is identified, the focus is on whether *this payment* is made *on the export*, and not on whether the source of the payment is dependent or contingent on export production”.⁸⁹

Accordingly, there is a clear difference between the terms “on the export” and contingent on export production. The facts of the case show that the payment – 50% of the blue box- granted to the swine producers is not contingent upon export performance, but rather related to the export. The EC-Sugar Panel established that “a payment “on export” need not be “contingent” on export but rather should be “in connection” with exports”.⁹⁰

88 See footnote 61.

89 Report of the Panel, EC-Sugar, para. 7.273.

90 Report of the Panel, EC-Sugar, para. 7.275.

As previously stated when analysing the SBS Scheme, this payment confers an advantage which is reflected in the favourable conditions upon which swine producers can export. Therefore, this payment and the benefit it confers is not due to a contingency on export –whether *de iure or de facto*- but by a process that encourages the export. Regarding the last requirement, the AB has established that “there must be a demonstrable link between the *governmental action* at issue and the *financing* of the payments”.⁹¹ The payment is granted by virtue of a governmental action.⁹²

It is clear that the PS fits the conditions and requirements to be understood as an export subsidy within the terms of articles 9.1 c of the AoA. Accordingly, such payments must have been included in the reduction commitments scheduled by Subsidia. This country has acted inconsistently with its obligations under article 9.1 c of the AoA.

2. Infringement of Articles 3.3 and 8 of the AoA

Competia has established that an export subsidy under Article 9.1 c of the AoA was not subject to reduction commitments. This fact constitutes a violation of Articles 3.3 and 8 of the AoA.

The infringement of the obligation expressed in Article 3.3 is the inconsistency to “not provide subsidies in respect of any agricultural product not specified in ... its Schedule”. Accordingly, the fact that Subsidia has provided an export subsidy that falls within the concept that previous Panel Reports⁹³ have adopted regarding article 9.1.c of the AoA, and that such a subsidy relies on an agricultural commodity not specified in the schedule –pork-, triggers the infringement.

The violation of Article 8 of the AoA is expressed by the inconsistency of Subsidia in “not to provide export subsidies otherwise than in conformity with [the *Agreement on Agriculture*] and with the commitments as specified in [its] Schedule”. Regarding this article, the EC-Sugar AB stated:

91 Appellate Body Report, Canada – Dairy (Article 21.5 II), para. 130; Appellate Body Report, Canada – Dairy (Article 21.5), para. 113.

92 Clarifications to the case. General Aspects.

93 Report of the Panel, US-Cotton, para. 7.748.

“...Members are prohibited from providing export subsidies otherwise than in conformity with the *Agreement on Agriculture* and the commitments as specified in their Schedules. Thus, compliance with both is obligatory. As compliance with the provisions of the *Agreement on Agriculture* is obligatory, it is clear that the commitments specified in a Member’s Schedule must be in conformity with the provisions of the Agreement. Only then would the export subsidies be in compliance with the requirements of Article 8”⁹⁴.

Subsidia is granting payments to commodities not specified in its commitments. Therefore, it did not schedule its export subsidy reduction commitments according to the AoA. Accordingly, the measures are inconsistent with articles 3.3 and 8 of the AoA.

3. Petition of Remedy

Competia has demonstrated that the payments under the PS Scheme are not blue box measures. Such subsidies must be included within the reduction commitments regarding export subsidies as established in Article 9.1 of the AoA. Therefore, by not following this provision, there is a clear violation of Articles 3.3 and 8 of the same treaty. Competia requests the Panel to rule that Subsidia brings its measures into compliance with the AoA.

Request for Remedies

Competia asks the Panel to recommend that the DSB requests Subsidia to bring its measures found to be inconsistent with Articles 3,6,8,9 of the AoA and Part III of the SCM into conformity with the obligations under these Agreements.

94 Apellate Body Report, EC-Sugar, para 216.

V. RESPONDENT'S WRITTEN SUBMISSION

On Submission to the Panel of the World Trade Organization
At The Centre William Rappard
Geneva, Switzerland
Elsa Moot Court Competition on wto Law 2005/2006
Dispute
Subsidia – Agricultural Subsidies on Sweet Biscuits, Wheat & Pork
Competia Vs. Subsidia
Submission of the Complainant Competia
January 2006

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5. General Agreement on Tariffs and Trade of 15 April 1994, LT/UR/A-1A/1/GATT/2.
6. Agreement on Textiles and Clothing of 15 April 1994, LT/UR/A-1A/11
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List of Abbreviations

| | |
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| AB | Appellate Body |
| AoA | Agreement on Agriculture |
| DSU | Dispute Settlement Understanding |
| GATT | General Agreement on Tariffs and Trade |
| PC | Peace Clause |
| PS | Pork Scheme |
| SB | Sweet Biscuits |
| SBM | Sweet Biscuits Manufacturers |
| SBS | Sweet Biscuits Scheme |
| SCM | Agreement on Subsidies and Countervailing Measures |
| WP | Wheat Producers |
| WTO | World Trade Organization |

WTO Agreement Marrakesh Agreement Establishing the
WTO

Statement of Facts

Subsidia is a developed WTO Member that has agreed to reduce its agricultural subsidies. Competia is a developing WTO member that has been assisted by Subsidia with economic development programs. Pressures from agricultural interests within Competia have reduced the level of diplomatic relations between these nations. Competia formally requested the formation of a WTO panel in order to address subsidies in three specific products: sweet biscuits, wheat, and pork

Subsidia produces sweet biscuits with expensive raw material. Accordingly, if its manufacturers produce with domestic ingredients, they are eligible to receive a subsidy that brings these ingredients to a competitive price. Subsidia developed a track system with the aim to follow up the final destination of the product allowing the government to determine if the manufacturer complies with the condition for the granting of the subsidy, which is the sell of the final product. Hence, once the condition is satisfied, the track system automatically determines if the manufacturer is entitled to receive the payment whether in the form of domestic support (if sold on the domestic market) or in the form of an export subsidy (if exported). Subsidia has scheduled its export reduction commitments and has not paid one Subsidian Cent beyond them.

Moreover, Subsidia provides price-contingent export subsidies to its wheat producers with the objective of protecting them from negative fluctuations in world market prices and demand. These payments do not exceed the commitments scheduled by Subsidia and have been reduced gradually by 36% during the ten years in which the subsidy has been in place. During that same period, Subsidia has grown its share of the world wheat market by about 5% each year reaching 39% in year 2004. Competia had 15% of the world market in 2002, enjoyed a growth of 9% in just one year, reaching an amount of 24%. In 2004 Competia had 20% of the world market of wheat.

Subsidia has effectively tried to limit swine production due to environmental concerns. Accordingly, it has scheduled a Blue Box measure – article 6.5 (a) (iii)-. In year 2000 9 million swine were produced in Subsidia, and by 2015 this number will be reduced to 7 million. Subsidian legislation has limited the amount of domestic support provided to each farmer under a complex calculation system in which they receive the same amount of subsidies

every year provided they cut production according to the plan made for each farm. If a farmer exceeds the number of heads in a given year, he loses 50% of his support payments for this year and the next one as well. All farmers –except for one who is in jail- are adequately implementing the plan.

Summary of Claims-

Wheat

Claim 1: The SCM Agreement does not apply to agricultural subsidies since the AoA brings specific rules dealing with subsidies on agricultural products, and thus, constitutes *lex specialis* that prevails over other provisions [SCM] regulating payments on this type of commodities. Accordingly Competia’s claim under Part III of the SCM has no basis, as this provision does not apply to agricultural subsidies.

Claim 2: Supposing this Panel considers that part III of the SCM Agreement does apply to agricultural subsidies, the presence of footnote 17 within this Agreement precludes the application of article 6.3(d) of the SCM to this type of subsidies, since agricultural subsidies are regulated by a specific set of rulings included in the AoA.

Claim 3: Subsidia does not cause serious prejudice to the interests of other Members because of an increase in its wheat world market share in the sense of paragraph 6.3 (d), since this phenomenon is not an effect of the granting of the subsidy.

Claim 4: Subsidia’s payments to wheat producers do not have the effect of depressing world market prices in the sense of paragraph 6.3 (c), since the payments granted to the recipients only allow them to sell at world market prices, and not at lower prices.

Claim 5: Even if the panel finds that the effect of Subsidia’s measure is an increase in the world market share in the sense of paragraph 6.3 (d) of the SCM, or a price depression in the sense of paragraph 6.3 (c), this is not sufficient to conclude that serious prejudice (article 5 (c) of the SCM) has arisen. The use of the word “may” in that paragraph determines that the proof of one of the situations in article 6.3 of that agreement only constitutes a possibility to find serious prejudice.

Sweet Biscuits

Claim 1: Subsidia's payments made under the SBS constitute either a domestic support or an export subsidy depending on the final destination of the product. As the granting of the subsidy is conditioned upon the sell of the product either on the domestic or on the export market, the payment will constitute a domestic support or an export subsidy depending on where the product is sold domestically or overseas.

Claim 1: Subsidia is providing subsidies under Article 9.1 (f), i.e., subsidies on agricultural products contingent on their incorporation in exported products. Since these types of subsidies only demand compliance with budgetary commitments, and Subsidia is in compliance with them, the responding Member is not in violation of its undertakings under Articles 3.3 and 8 of the AoA.

Pork

Claim 1: The PS constitutes a Blue Box measure since payments made to swine producers are contingent upon a product limitation program. This program is being successfully executed because every swine producer, but one, is complying with the reducing plan made out for each farm.

Claim 2: Even if this Panel is of the view that Subsidia's payments to swine producers do not constitute a Blue Box domestic support, it could not be asserted that those payments constitute export subsidies in the sense of Article 9.1 (c) of the AoA since they do not have a spill over effect on the export market.

Arguments

II. Regarding Wheat-

1. Part III of the SCM does not apply to agricultural subsidies

Competia considers that Subsidia's agricultural subsidies to wheat producers violate part III of the SCM Agreement¹. However, the claimant does not take into account the fact that the SCM does not apply to agricultural subsidies since the AoA brings specific provisions dealing with agricultural goods. Additionally, footnote seventeen of the SCM inhibits the application of

1 Facts of the case. Terms of Reference Box.

Article 6.3(d) of the SCM to the AoA since this Agreement provides multilaterally agreed specific rules regarding agriculture.

1.1 The AoA is *Specialis* that prevails over the SCM

The AoA provides special rules dealing with agricultural domestic support and export subsidies, excluding the application of SCM rules in this issue. This assertion has its basis on the interpretation of article 21.1 of the AoA that provides as follows:

*“The provisions of GATT 1994 and other Multilateral Trade Agreements in Annex 1A to the WTO Agreement shall apply subject to the provisions of this Agreement.”*²

While analysing the EC-Bananas case, the AB held that Article 21.1 stipulates that GATT 1994 and other Annex 1A agreements apply to agricultural subsidies “*except to the extent that the AoA contained specific provisions dealing specifically with the same matter*”.³ Regarding the latter, it shall be understood that when the AoA deals with specific provisions such as agricultural subsidies, it excludes the application of the SCM to the same matter.⁴

This interpretation is consistent with the fact that within the WTO agricultural products are given a special treatment, with a specific set of rules and a different legal regime. As explained by Didier Chambovey, “within the WTO context, agricultural products are given a special treatment since they are covered by a sectoral [bis] agreement negotiated separately from the SCM agreement, on different assumptions and in pursuit of different objectives”.⁵ This allows the AoA to be *lex specialis*, and thus, it prevails over the SCM Agreement.

2 Agreement on Agriculture of 15 April 1994, LT/UR/A-1A/2, Article 21.1.

3 Report of the Appellate Body, *European Communities- Regime for the importation, Sale and Distribution of Bananas*, WT/DS27/AB/R, 9 September 1997, paras. 155-158.

4 Didier Chambovey, “How the Expiry of the Peace Clause (Article 13 of the WTO Agreement on Agriculture) Might Alter Disciplines on Agricultural Subsidies in the WTO Framework”, *Journal of World Trade*, 36(2) (2002), 305-352 (page 309).

5 Didier Chambovey, “How the Expiry of the Peace Clause...”, p. 309 and 310

Furthermore, a cumulative application of both covered agreements would result in contravention of the AoA's negotiation history and the principle of *in dubio mitius*.⁶ The AB has stressed that negotiation of special rules for agricultural products was made in order to provide less onerous provisions for these commodities than those applicable to all other goods.⁷ Hence, to apply the AoA and the SCM cumulatively would submit agricultural subsidies to more severe rules than those applying to other type of subsidies.⁸

One last argument that supports the non-application of the SCM to agricultural subsidies is that, if the intention of the negotiators were to integrate both agreements upon the expiration of the peace clause, the AoA would have included an express provision establishing this situation. This was the case of the Agreement on textiles and Clothing and GATT 1994.⁹

For the reasons expressed above, Subsidia alleges that SCM provisions do not apply to agricultural subsidies. Therefore, the AoA is the relevant agreement to determine any violation in the present case. Since Subsidia is in full compliance with its reduction commitments the export subsidies to wheat producers are in consonance with the WTO.

1.2 Article 6.3(d) of the SCM does not apply to agricultural subsidies due to footnote seventeen

Supposing this Panel considers that part III of the SCM Agreement does apply to agricultural subsidies, the presence of footnote 17 within this Agreement precludes the application of article 6.3(d) of the SCM to this

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- 6 According to this principle “[i]f the meaning of a term is ambiguous, that meaning is to be preferred which or less onerous to the party assuming an obligation, or which interferes less with the territorial and personal supremacy of a party, or involves less general restrictions upon the parties”. Didier Chambovey, “How the Expiry of the Peace Clause...”, page 310, quoting R. Jennings and A. Watts (eds). *Oppenheim's International Law*. 9th edition, vol. 1. Longman, London, 1992, p. 1278
- 7 Report of the Appellate Body, *European Communities- Measures concerning Meat and Meat Products (Hormones)*, WT/DS26/AB/R, 16 January 1996, para. 165.
- 8 Didier Chambovey, “How the Expiry of the Peace Clause...”, page 310.
- 9 David Morgan and Goh Gavin, “Peace in Our Time, An Analysis of Article 13 of the Agreement on Agriculture”, *Journal of World Trade*, 37(5) (2003), 997-992 (p. 987). Agreement on Textiles and Clothing of 15 April 1994, LT/UR/A-1A/11, Preamble: “...negotiations in the area of textiles and clothing shall aim to formulate modalities that would permit the eventual integration of this sector into GATT ...”

type of subsidies, because they are regulated by a specific set of rulings included in the AoA.

Article 6.3 of the SCM states that “Serious prejudice in the sense of paragraph (c) of Article 5 *may* arise in any case where one or several of the following apply...”

(d) the effect of the subsidy is an increase in the world market share of the subsidizing Member in a particular subsidized primary product¹⁰ or commodity¹¹ as compared to the average share it had during the previous period of three years and this increase follows a consistent trend over a period when subsidies have been granted.”¹²

As it can be regarded from the footnote, a claim under article 6.3 (d) can be submitted unless other multilaterally agreed specific rules apply to the trade of the product or commodity in question. The AoA is a multilateral trade agreement that provides specific rules to agricultural products, therefore it falls within the provision of footnote seventeen.

Accordingly, a claim that a subsidy to wheat producers causes serious prejudice because it fulfils the requirements in article 6.3 (d) would be unsustainable.

It must be noted that in relation to article 6.3 (d) there has been no ruling from WTO Panels and the AB. Although in the US-Cotton case Brazil brought a claim against the US arguing that the subsidies provided by this country were causing serious prejudice because of an increase in its world market share, the Panel did not rule if footnote seventeen of the SCM applied to agricultural subsidies since Brazil did not make a *prima facie* case.¹³

10 Understanding primary product as any product of farm, forest or fishery, or any mineral, in its natural form or which has undergone such processing as is customarily required to prepare it for marketing in substantial volume in international trade. General Agreement on Tariffs and Trade 1947, *Ad Article XVI Section B*.

11 “Unless other multilaterally agreed specific rules apply to the trade in the product or commodity in question”. SCM Agreement of 15 April 1994, LT/UR/A-1A/9, footnote seventeen.

12 SCM Agreement, Article 6.3 (d).

13 Report of the Panel, *United States Subsidies on Upland Cotton*, WT/DS267/R, 8 September 2004, para 7.1464.

2. Subsidies Regarding Wheat

Subsidia's price contingent export subsidies to wheat producers do not violate part III of the SCM. In order to prove this, the Respondent will first analyse how there is no basis to support a claim under Article 5 (a) and (b) of the SCM. Subsequently, Subsidia will establish how its price contingent export subsidies do not cause serious prejudice in the sense of Article 5(c) and 6.3 (a), (b), (c) or (d) of the SCM, making special emphasis on the claims regarding the increase in the world market share and the price undercutting. Finally, Subsidia will demonstrate how the proof of one of the situations in paragraph 6.3 does not suffice to prove serious prejudice according to Article 5 (c) of the same Agreement.

2.1 Subsidian Measures do not cause adverse effects to the interests of another Member in the sense of Article 5 (a) and (b) of the SCM

Subsidia considers that in this case there is not basis to present a claim arguing adverse effects neither in the form of injury to the domestic industry of another member, nor in the way of nullification or impairment as established in Articles 5 (a) and (b) respectively. Thus, Subsidia will defend its measure from a claim of serious prejudice in the sense of Article 5 (c) of the SCM.

Part III of the SCM refers to legal Subsidies that may be actionable when they cause adverse effects to the interests of other Members. In doing so, article 5 of such Agreement provides three situations whereby it is understood that adverse effects arise. The first event occurs when injury to the domestic industry of another member is caused; the second, when nullification or impairment of the benefits accruing directly or indirectly to other Members under GATT 1994 happens; and finally, whenever a member causes serious prejudice to the interests of another member.¹⁴

According to the facts of the case there is no basis to claim adverse effects under paragraphs 5(a) or 5(b) of the SCM Agreement. First, article 5 (a) provides that the term "injury to the domestic industry" needs to be used in the same sense as in part V the same agreement. This part refers to *injury through subsidized imports*, which requires data of importation amounts as well as the effect they have over domestic prices¹⁵. The latter does not fit within the facts of this case.

14 SCM Agreement, Article 5.

15 SCM Agreement, Part V, Article 15.

Regarding Article 5 (b) –nullification or impairment–, GATT/WTO Panels have identified three requirements in order to raise a claim under this provision¹⁶. First, that a tariff concession has been negotiated under GATT and resulted mandatory to the member. Second, that after the entry into force of this binding, a subsidy scheme was introduced in the territory of the same member. Finally, that the subsidy nullifies or impairs the benefits accruing to the country profiting from the tariff, due to the fact that the subsidy scheme went against the legitimate expectations of the addressee of the promise¹⁷. From the facts of the case it is not possible to assert that one of the three requirements exists.

Once Subsidia has explained the reasons why a claim under articles 5 (a) and (b) is not possible, it will focus its defence in arguing that the measure at issue does not constitute serious prejudice to the interests of another member in the sense of article 5 (c) of the SCM.

2.2 Subsidia's measure does not cause serious prejudice in the sense of paragraph 6.3 (d) and (c) of the SCM Agreement

Article 6.3 of the SCM establishes four situations in which serious prejudice in the sense of article 5 (c) of the same Agreement *may* arise¹⁸. Since there is no information in order to base a claim under articles 6.3 (a) or (b) of the SCM¹⁹, Subsidia will base its defence arguing that the measure does not fit within the situation described in article 6.3 (d) or (c) therein.

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- 16 GATT Panel Report, *Australian Subsidy on Ammonium Sulphate*, BISD II/188, 3 April 1950, esp. para 12. GATT Panel Report, *Treatment by Germany of Imports of sardines*, G/26, 1S/53, 31 October 1952, esp. para 16. Interpretations of GATT Article XXIII: 1 (b) apply to Article 5 (b) of the SCM because the term nullification or impairment is used in the same way in both provisions. (SCM Agreement article 5 (b) footnote 17)
- 17 Mitsuo Matsushita, *World Trade Organization: Law and Practice*. (Oxford International Law Library 2003), p. 278-279.
- 18 Subsidia will not address the four situations described in paragraph 6.1, since they have already expired according to article 31 of the SCM Agreement.
- 19 As the US-Cotton Panel has stated, Articles 6.3(a) and (b) of the SCM Agreement each identify a particular “market” and a particular trade flow. They refer, respectively to: “imports into” “the market of the subsidizing Member”; and “exports” from “a third. Report of the Panel, *US-Cotton*, para. 7.1239. Hence, in order to raise a claim under these Articles it would be necessary to have either the data of the imports in one country, or a third country market, and this information does not exist in this case.

2.2.1 Subsidian measure does not fit in the situation described in paragraph 6.3 (d) of the SCM

Although Article 6.3 (d) of the SCM does not apply to agricultural subsidies (see above I.2), Subsidia will strengthen its defence by demonstrating that there is no substantial relationship between the granting of the subsidy and the increase in Subsidia's world market share. Therefore, this case does not fall within the situation described in Article 6.3(d) of the SCM Agreement.

Article 6.3 (d) of the Agreement in question establishes that serious prejudice may arise whenever "the effect of the subsidy is an increase in the world market share of the subsidizing Member (...)".²⁰ The AB has suggested the meaning of the phrase "the effect of the subsidy" as the necessity for the claimant to prove a "genuine and substantial relationship of cause and effect" between the granting of the payment and the consequence alleged (i.e. increase in the world market share). Likewise, the AB has stressed that the effect of other factors play a determinant role in the assessment of the casual link.²¹ Regarding the latter, Subsidia will explain how its increase in the wheat world market share also obeys to other factors and not to the price contingent export subsidy exclusively.

The effect of Subsidia's measure is not an increase in the wheat world market share, even though the facts of the case show that the defendant has increased its share in the wheat market. It shall be noted that the mere fact that a country has increased its market share, does not mean that this situation takes place necessarily because of the country's export subsidies.

In other words, the fact that a country increased its world market share does not mean that this has occurred as a result of the implementation of a subsidy, since there are many other factors different from subsidies that may explain the shifts in market shares. Accordingly, wheat world market share may have been influenced by the reduction of competition from other exporters,²² by a shift in productive capacity in third countries,²³ by an increase of

20 SCM Agreement, part III, Article 6.

21 Appellate Body Report, *US-Cotton*, paras. 437-438.

22 GATT Panel Report, *European Communities Refunds of Exports of Sugar, L/5011-27S/69*, 6 November 1979, para. 4.13.

23 GATT Panel Report, *European Economic Community-Subsidies on export of Wheat Flour*, SCM/42, 21 March 1983.

demand in Competia or another country, etc; and not necessarily because of Subsidia's price-contingent export subsidies.

To illustrate the above assertion Subsidia would like to recall the *EC-Wheat Flour* GATT case, where the Panel did not rule against the European Communities increase in the world market share, sine the existence of different factors in the wheat market influenced the changes in shares. *Inter Alia*, the Panel mentioned the occurrence of political embargoes; the fact that Europe had a better geographical position than the US to supply markets such as Africa or Middle East countries –“regular shipping lines”–; dietary demands; product quality considerations, etc.²⁴

Agricultural markets are complex and may be influenced by many factors²⁵, something that charges the claimant with the burden of proving the existence of a substantial link between the subsidy and the increase in the world market share, and not simply the increase in the world market share during the period in which the subsidy has been in place.

Moreover, the fact that the defendant has reduced its export subsidies by an amount of 36% with no consequence over the increase in the world market share,²⁶ shows how the subsidy has minimal or no effects over the shifts in the world market share. In other words, if the subsidy had the effect of increasing the world market share, its reduction would have had the effect of decreasing the share it had gained, something that does not happen in this case. This determines that the casual link between Subsidia's gain in the world market share and the granting of the payment is not tight enough so as to reveal that the former is the effect of the latter.

For the above-mentioned arguments Subsidia's measure does not fit in the situation described in article 6.3 (d) of the SCM Agreement.

24 GATT Panel Report, *EEC-Wheat Flour*, paras 4.20 – 4.24.

25 Richard H. Steimberg and Timothy E. Fosling, “When the Peace Ends: The Vulnerability of EC and US Agricultural Subsidies to WTO Legal Challenges”, *Journal of International Economic Law*, 6 (2) (2003), 369-417 (p. 384).

26 Facts of the case, para. 10.

2.2.2. Subsidian measures do not constitute a significant Price Undercutting, price suppression, price depression or lost sales in the same market

In order to establish that Subsidian payments do not have the effect described in article 6.3 (c), the defendant will demonstrate that the amount paid to wheat producers only brings the price of domestic wheat to world market rates, and not below that quantity.

According to the US-Cotton Panel, *price suppression* refers to the situation where prices either are prevented or inhibited from rising or they do actually increase, but the increase is less than it otherwise would have been. *Price depression* refers to the situation where prices are pressed down, or reduced.²⁷

Regarding the design of the measure, Subsidia provides price-contingent export subsidies in order to ensure that wheat farmers are not adversely affected by fluctuations in world market price and demand.²⁸ In pursuing this objective, Subsidia pays an amount of money whenever the world market price has the effect of placing Subsidian producers in an adverse position to compete, i.e., when the world market price is lower than the domestic price. Accordingly, Subsidia is trying to protect its producers from market externalities (as it may be the negative subsidy from another member creating price depression), negative fluctuations in demand, etc.

The effect of this subsidy is to bring wheat producers back to competition by allowing them to sell at world market prices. This situation results in Subsidian producers being able to sell at the same price as other market competitors and not at a lower price. The latter means that since Subsidian producers cannot sell the wheat at prices lower than the ones paid for the same commodity in the world market, it is not possible for the subsidy to have the effect of price undercutting, depression, suppression or lost sales in the world market price.

Also, this situation only assures wheat producers that they are going to continue in the market, but it does not promote more domestic production because the subsidy does not provide any price advantage overseas. In this way, since Subsidian wheat is not more attractive to foreign buyers, the demand of the product would remain stable and therefore the supply would

27 Panel Report. US-Cotton, para. 7.1276.

28 Facts of the case, para 9.

remain stable as well.²⁹ The latter proves that Subsidia is not creating overproduction on the wheat market, what is usually seen by Scholars as another source of price depression.³⁰

For the above-mentioned arguments Subsidia's price contingent export subsidies do not have the effect of a significant price undercutting, depression, suppression or lost sales in the world market price for wheat in the sense of Article 6.3(c) of the

2.3 The demonstration of one or more of the items in paragraph 6.3 is not sufficient to prove serious prejudice

Subsidia has demonstrated that the export subsidies provided to its wheat producers do not fit within the situations described in Articles 6.3(c) and (d) of the SCM. Consequently, Subsidia will establish that even if the Panel considers that the price-contingent export subsidies have the effect of an increase in the world market share or the effect of price undercutting, the demonstration of the situations described in articles 6.3 (c) and/or (d) is not enough to prove serious prejudice in the sense of article 5 (c).

This assertion has its rationale in the chapeau of article 6.3 which provides that "*Serious prejudice in the sense of paragraph (c) of Article 5 may arise in any case where one or several of the following apply*". (underlining added). The meaning of the term "may" used in this provision has been a determining factor to conclude the effect of proving one of the items in this paragraph.

Subsidia considers that this Panel should disregard the interpretation given by the US-Cotton Panel of the word "may"³¹. According to article 31.1 of

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- 29 The above-mentioned proves that the export subsidy provided to producer does not pretend to cause a shift in the equilibrium of demand and supply on the market of wheat.
- 30 "An increase in supply without a change in demand causes the price to fall and the quantity demanded to rise." Roy J. Ruffin and Paul R. Gregory, *Principles of Economics*, 5th edn (Addison Wesley Longman 2001) p. 74.
- 31 We therefore do not believe that once we have concluded that the conditions in article 6.3 (c) are fulfilled, and thus that serious prejudice "in the sense of paragraph c of article 5 "may" arise, a separate examination of the existence of "serious prejudice" under the chapeau of article 6.3 or article 5 (c) is necessary. Report of the Panel, *US-Cotton*, para. 7.1389.

the Vienna Convention “A treaty shall be interpreted in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose”.³² Accordingly, if the ordinary meaning of the term “may” is “possibility” or “permission”, the chapeau of article 6.3 is meant to say that whenever it is proven that one of the situations in this article has arisen, there is a possibility to demonstrate that serious prejudice in the sense of article 5 (c) exists. Hence, the article never meant to say that whenever a claimant proved one of these situations serious prejudice exists.

Furthermore, if members had intended an interpretation in which the demonstration of one of the items in article 6.3 was sufficient to raise serious prejudice, they would have used a different word like they did in paragraph 6.1 where they employed the term “shall”. It should also be taken into account the fact that, even if the panel in US-Cotton made a different interpretation regarding the word “may” in the chapeau of article 6.3 and the AB did not reverse this interpretation, this does not preclude this Panel’s analysis from making a different finding. The latter has its basis on the fact that adopted Panel or AB reports are not binding precedent and do not control subsequent panels.³³

To sum up, whenever a Member demonstrates that one of the situations described in article 6.3 has occurred, it still has to demonstrate that serious prejudice in the sense of article 5 (c) of the SCM has arisen, since the very proof of one of the items in 6.3 does not constitute *per se* serious prejudice to the interests of another member.

3. Conclusion

For all the reasons stated above, Subsidia requests the Panel to dismiss Competia’s claims since it did not cause serious prejudice in the sense of article 5 (c) of the SCM through article 6.3 paragraphs (c) or (d), and therefore it did not violated part III of the SCM Agreement.

32 Vienna Convention on the Law of Treaties of 23 May 1969, I.L.M 8 (1969), 679, Article 31.1.

33 Appellate Body Report, *Japan - Taxes on Alcoholic Beverages*, WT/DS10/AB/R, WT/DS11/AB/R, 4 October 1996, p. 12. See also, Mitsuo Matsushita, *World Trade Organization*, p. 58.

III. Regarding Sweet Biscuits.

1. Legal Arguments

Subsidia will prove that payments made under sweet biscuits scheme constitute either a domestic support or an export subsidy depending on the final destination of the product. The export subsidy is notified as a “subsidy on agricultural products contingent on their incorporation in exported products” under art. 9.1.f of the AoA, and due to its nature it only demands the compliance with budgetary outlay commitments. Thus, considering that Subsidia has fully met its budgetary commitments³⁴, the Respondent Member is in compliance with its undertakings under articles 3.3 and 8 of the AoA.

1.1 Sweet biscuits scheme is a twofold nature measure

Payments made under SBS are either domestic support or export subsidies depending on the final destination of the product. To prove the latter, in the following subsections Subsidia will explain the architecture and design of the measure, and then, will compare the measure with the *user marketing (Step 2) payment* assessed by the Panel in Us-Cotton case.

1.1.1. Architecture and design of the measure

The SBS has a dual nature and its understanding must be approached by dividing its design in two stages: when the payment is decided and when the subsidy is granted. Thus, the granting of the subsidy is determined by the final destination of the product which is established because of the track system.

The SBS has a twofold aim: (1) to work as an outlet for domestic raw material; and (2) to allow sweet biscuits manufacturers to be competitive.³⁵ Following these objectives, Subsidia has established a measure of dual nature depending on the final destination of the product. The establishment of the product’s final destination is achieved thanks to the track system that oversees if the products are sold on the domestic or export markets.³⁶

34 Facts of the Case, para. 9.

35 Facts of the Case, para. 5.

36 Facts of the Case, para. 6.

The scheme discerns between the moments when the payment is decided and when the subsidy is granted.³⁷ The first moment of the scheme occurs when the manufacturer proves to the government that it produced sweet biscuits with domestic sugar, butter and wheat flour.³⁸ As a result, the government decides to pay the subsidy. The second moment occurs when the final product, with incorporated raw material, is tracked by the system as a commodity sold in the domestic market or exported. If the latter occurs, the manufacturer is entitled to receive the payment, which shall be granted by the Government. All this being considered, is easy to see how the tracking system plays a central role determining whether the payment is a domestic support or an export subsidy.

1.1.2. The Dual nature of the Sweet Biscuits measure

The Panel in US-Cotton analysed the scheme designed by the United States known as *user marketing (Step 2) payments*, concluding that such payments given under this system constituted a domestic support or an export subsidy. Considering the similarities between the US Scheme and the SBS, Subsidia will prove the twofold nature of its measure based on the findings of the Panel in the case mentioned.

There are a number of similarities between the *user marketing (Step 2) payments* and the Sweet Biscuits scheme. The Panel in US-Cotton depicted the characteristics of the measure as follows:

We further agree that, pursuant to the legislation and regulations, the form and rate of payment to domestic users and exporters are identical; and the fund from which payments are made is a unified fund available to both eligible domestic users and exporters. We acknowledge that, as the United States argues, upland cotton does not have to be exported in order to trigger eligibility for a user marketing (Step 2) payment under

37 The Panel in Us-Cotton analysed the difference between two moments in the payment of a subsidy as follows: “*Decided*” refers to what the government determines, but “*grant*” refers to what its measures provide. Report of the Panel, *Us-Cotton*, para. 7.746, statement confirmed by the Appellate Body Report, para. 382. Although the Panel stated this whilst analyzing the meaning of article 13(b)(ii) of the AoA, Subsidia considers that the distinction is useful to understand the scheme and the moment when the transaction of monetary funds (granting of the subsidy) takes place.

38 Clarifications to the case, Introduction to Sweet Biscuits.

section 1207(a) as domestic users are also eligible (i.e. for a payment to a *domestic user*)³⁹.

Establishing a parallel between the characteristics of the measure quoted above and the characteristics of the SBS, it may be regarded, first, that the form and rate of payments to domestic users and exporters are identical in the two schemes. Second, the fund from which payments are made is a unified fund available both to eligible domestic users and exporters, as it happens in the two systems. Finally, sweet biscuits do not have to be exported in order to receive the payment because there is the possibility to access to it through the domestic support scheme.⁴⁰

However, the most important elements of the *user marketing (Step 2) payment* (which are similar to Sweet Biscuits scheme as explained below) are the ones that allowed the Panel to conclude that the measure must be analysed in two scenarios. These elements are the final destination of the product and the proof required for the granting of the subsidy.

Regarding the first element, the Panel in *US-Cotton* stated that the final destination of the product is conclusive to find the nature of the measure. This was addressed as follows,

A bale of United States domestically produced upland cotton must *either* be exported to trigger receipt of a user marketing (Step 2) export payment, *or* purchased for domestic use to trigger receipt of a user marketing (Step 2) domestic payment. The two situations must be distinct as the same bale of cotton cannot be exported and also sold to a domestic user.⁴¹

In this case, internal production of sweet biscuits (with incorporated raw material) must either be exported to trigger a sweet biscuits export payment, or be sold on the domestic market to trigger a sweet biscuits domestic support. The latter compels the Panel to examine separately in this case the

39 Report of the Panel, *Us-Cotton*, para. 7.709.

40 This can be concluded regarding the clarifications to the case, Introduction to Sweet Biscuits, that state: “[a]ll the sweet biscuits manufacturers get subsidies if they produce with domestic ingredients”. See also, Facts of the Case, para. 5: “[t]hese subsidies are set at an amount that brings the price of these ingredients to the level of market prices...”.

41 Report of the Panel, *Us-Cotton*, para. 7.723.

conditions pertaining the granting of the subsidy involving two different eligible recipients: sweet biscuits manufacturers who sell on the domestic market and manufacturers who sell on the export market.⁴²

Considering the second element that permitted the Panel to find out the dual nature of the measure in the US-Cotton case, this Panel stated:

We note further that a distinction is drawn in the measure itself between domestic users and exporters in terms of the proof needed to be eligible for the subsidy: domestic users are eligible upon proof of opening a bale, and exporters are eligible upon proof of export.⁴³

Therefore, the proof needed for the granting of the subsidy in the SBS is determined by the support of the track system which has the function to establish whether sweet biscuits were sold on the domestic market or exported.⁴⁴

For the reasons stated above, and supported in the considerations upheld by the Panel in *Us-Cotton*, the Respondent Member considers that its SBS, related to the granting of the subsidy, has a dual nature: domestic support or export subsidy.

1.2 Proving the existence of an export subsidy under art. 9.1.f of the AoA

So far Subsidia has demonstrated the dual nature of the SBS. This section will focus on the exports scenario by proving that the payments provided to its sweet biscuits manufacturers constitute an export subsidy under art. 9.1.f of the AoA because it complies with the elements required therein.

Article 9.1.f sets forth that:

1. The following export subsidies are subject to reduction commitments under this Agreement:

42 Report of the Panel, *Us-Cotton*, para. 7.724.

43 Report of the Panel, *Us-Cotton*, para. 7.726.

44 Facts of the Case, para. 6. Although, the difference on the proof in marketing (Step 2) payment was related to the eligibility, in Sweet Biscuits is related to the granting of the subsidy. Regarding the distinction between the moment of deciding and granting the subsidy (see above).

f) Subsidies on agricultural products contingent on their incorporation in exported products.

Customary rules of interpretation of international law provide that treaties shall be interpreted “in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose”.⁴⁵ In application of this, Subsidia considers that the ordinary meaning of the text allows the interpreter to conclude that there are two necessary elements to prove the existence of a subsidy under art. 9.1.f: (i) subsidy on agricultural products, and (ii) contingent on their incorporation in exported products. Accordingly, Subsidia will establish these two elements under the SBS.

1.2.1. Subsidy with benefits on agricultural products

Payments made to sweet biscuits manufacturers confer a benefit to the producers of domestic sugar, butter, and wheat flour, proving that the subsidy is “on agricultural products”.

This effect, known as “pass-through”,⁴⁶ has been previously interpreted by WTO Panels as follows:

Export-contingent subsidies need not be made solely to producers of the product concerned. To the extent a subsidy made to a purchaser of the product enables that purchaser to obtain that product on more favourable terms than would otherwise be available in the marketplace, *this will, at a minimum, represent a prima facie case that the payments confer a benefit on the producers of that product as well*, as it lowers the cost of the product to their purchasers and thus makes their product more attractive relative to competing products”.⁴⁷ (emphasis added)

45 Vienna Convention on the Law of Treaties, art. 31.1; Report of the Panel, *Us-Cotton*, para. 7.965.

46 Appellate Body Report, *Final Countervailing Duty Determination with Respect to Certain Softwood Lumber from Canada*, WT/DS257/AB/R, 19 January 2004, para. 146.

47 Report of the Panel, *Us-Cotton*, footnote 898; Report of the Panel, *Canada - Export Credits and Loan Guarantees for Regional Aircraft*, WT/DS222/R, 28 January 2002, para. 7.229; Panel Report; Report of the Panel, *Brazil - Export Financing Programme for Aircraft - Second Recourse by Canada to Article 21.5 of the DSU*, WT/DS46/RW/2, 26 July 2001, para. 5.28.

Therefore, Subsidia's way to achieve the outlet for domestic raw material is through a payment provided to sweet biscuits manufacturers' contingent upon the incorporation of domestic raw material to its product.⁴⁸ This payment pretends to bring the price of these ingredients at a competitive price⁴⁹, which proves that domestic agricultural producers of sugar, butter and wheat flour are receiving a benefit through the payment made to sweet biscuits manufacturers.

Thus, considering that the subsidy under the SBS confers a benefit to domestic raw material producers, Subsidia concludes that the payment under study is on the agricultural products as required by art. 9.1.f of the AoA.

1.2.2 Contingent on the incorporation in exported products

Also, payments provided under SBS are contingent on the incorporation of domestic sugar, butter, and wheat to the exported product. Two reasons support the latter: the distinction between the moment when the payment is decided or granted and the application of the International Accounting Standards on Agriculture (IAS 41).

At the outset, in order to assess the export contingency on incorporated products, the primary issue is to understand that the export subsidy provided under the SBS is composed of two different moments that require two different kinds of proofs.

The first moment in the SBS occurs when the manufacturer purchases domestic ingredients⁵⁰ and proves to the government the incorporation of the raw material on the sweet biscuits production.⁵¹ At this point, the subsidy is decided according to the incorporation of the product, though the contingency on export is still standing.⁵² The second moment occurs when

48 Clarifications to the case, Introduction to Sweet Biscuits.

49 Facts of the Case, para. 5.

50 Facts of the Case, para. 5.

51 Clarifications to the case, Introduction to Sweet Biscuits.

52 Sweet Biscuits Scheme works similar to the scheme of The EC Common Organization of the Market in Wine described on the Council Regulation (EC) No. 1493/1999 of 17 May 1999. The EC Regime on Wine distinguishes between the moment when the manufacturer qualifies for the subsidy and the moment when the refund shall be paid, and establishes different proofs regarding the moment. Regarding the first part art. 64.2 of the Regulation (EC) No. 1493/1999 states that "[t]o qualify for the refund,

the condition of sale of the product on the export market is met. Here, the manufacturer is entitled to demand the payment of the export subsidy from the Government. Regarding the burden of proof required in this part, the government has established a tracking system which establishes automatically that the product was in fact exported. The latter eases the burden of proof to the manufacturers.⁵³

On the other hand, the SBS is divided in two moments obeying to the International Accounting Standards on Agriculture (IAS 41) which establish that:

“an unconditional government grant related to a biological asset measured at its fair value less estimated point-of-sale costs should be recognised as income when the government grant becomes receivable. *If a government grant related to a biological asset measured at its fair value less estimated point-of-sale costs is conditional, including where a government grant requires an enterprise not to engage in specified agricultural activity, an enterprise should recognise the government grant as income when the conditions attaching to the government grant are met...*”.⁵⁴ (emphasis added).

As a result, sweet biscuits manufacturer can only recognise the government grant as an income once the condition is complied. As above-mentioned, the condition for the granting of the export subsidy is the sale of the product on the market and not the incorporation of the raw material in the sweet biscuit. Given the case that the manufacturer will incorporate the income on his balance sheet at the moment the subsidy is decided and not when it is

processed products must, on export, be accompanied by a declaration from the applicant indicating the amounts of raw sugar, white sugar, glucose and glucose syrup used in their manufacture”.

- 53 Regarding the second moment of the EC Regime on Wine, Regulation (EC) No. 1493/1999 stipulates in art. 64.6 that the refund shall be paid on the proof that the products have been exported and reached the destination mentioned on the export license. As explained above, Subsidia has preferred to help manufacturers in the compliance of this proof through the establishment of the tracking system.
- 54 IASB, *International Accounting Standards 41*. February 2001, para. 34.

received or receivable, he or she will be infringing the basic accountancy principle of “Revenue Recognition”.⁵⁵

For all the reasons expressed above, Subsidia has demonstrated that the subsidy provided under SBS is contingent on the incorporation of domestic sugar, butter and wheat to the exported product. What is more, Subsidia has demonstrated that the subsidy provided falls within the scope of art. 9.1.f of the AoA.

1.3 Subsidia is in compliance with its Budgetary Outlays Commitments and arts

3.3 and 8 of the AoA

The subsequent practice of Member States has demonstrated that reduction commitments in export subsidies under art. 9.1.f are only subject to reduction on budgetary outlays. Therefore, Subsidia is complying with its reduction commitments under arts. 3.3 and 8 of the AoA.

Regarding the content of arts. 3.3 and 8 of the AoA, the Appellate Body in EC-Sugar has established that:

(...) [a]rticle 3.3 requires a Member to schedule both budgetary outlay and quantity commitment levels in respect of export subsidies listed in Article 9.1 of the *Agreement of Agriculture*.⁵⁶

It added:

It is clear from the plain wording of Article 8 that Members are prohibited from providing export subsidies otherwise than in conformity with the *Agreement on Agriculture* and the commitments as specified in their Schedules.⁵⁷

55 “The Revenue Recognition Principle states that revenues are recorded when main criteria has been met: (1) The earnings process is substantially complete, generally, a sale has been made or services have been performed. (2) Cash has been collected or collectibility is reasonably assured”. W. Steve Albrecht and others. *Financial Accounting*, 9th edn (Ed. Thomson Southwestern 2005), p. 142. See also, Larry Wlather. *Principles of Accounting*. Chapter 3. <http://www.principlesofaccounting.com> [accessed 21 december 2005].

56 Appellate Body Report, *EC-Sugar*, para. 200.

57 Appellate Body Report. *EC-Sugar*, para. 216.

Nonetheless these two articles must be interpreted in conformity with the rules of Vienna Convention on the Law of Treaties, especially in relation to art. 31.3.b which establishes that treaties should be interpreted taking into account together with the context:

“(b) any subsequent practice in the application of the treaty which establishes the agreement of the parties regarding its interpretation”.

Regarding the above, it does exist a subsequent practice among WTO Members to comply with export subsidies reductions commitments on incorporated products just on the basis of budgetary outlays.⁵⁸ This practice is supported by the Uruguay Round negotiations document known as “Modalities Paper”,⁵⁹ which establishes some guidelines in relation to how to schedule subsidies reduction commitments in the correct manner.⁶⁰

Moreover, the Panel has recognised that “the so-called Modalities Paper is not a covered agreement and thus cannot provide for WTO rights and obligations to Members. Nonetheless, it could be relevant when interpreting the *Agreement on Agriculture*, including Members’ Schedules”.⁶¹

Consequently, Subsidia considers that its reduction commitments on sweet biscuits must be read at the light of the Modalities Paper content.

58 See, WTO. http://www.wto.org/english/tratop_e/agric_e/ag_intro04_export_e.htm#reduction [accessed 30 december 2005]; Europe Communities and Canada Reduction Commitments at WTO. http://www.wto.org/english/tratop_e/schedules_e/goods_schedules_e.htm [accessed 30 december 2005].

59 Modalities for the Establishment of Specific Binding Commitments, Note by the Chairman of the Market Access Group, MTN.GNG/MA/W/24, 20 December 1993, paragraph 9 of Annex 8.

60 Raj Bhala, “World Agricultural Trade in Purgatory: The Uruguay Round Agriculture Agreement and its Implications for the Doha Round”, *North Dakota Law Review*, 71-291 (2003), 691-828 (p. 727). NAFTA Agreement. Arbitral Panel Established Pursuant to Article 2008, Final Report of the Panel. *Matter of Tariffs applied by Canada to Certain U.S – Origin Agricultural Products*, CDA-95-2008-01. 2 december 1996, cited by Raj Bhala, *International Trade Law: Theory and Practice*, 2nd edn (Lexis Publishing 2001), p. 707.

61 Panel Report. *EC-Sugar*, para. 7.350.

1.3.1. Legal Issue Applied to the facts of the case

Subsidia has scheduled commitments under budgetary outlays and quantities commitments. However, its compliance with arts. 3.3 and 8 of the AoA must be analysed solely on the basis of budgetary outlays.

According to the facts, Subsidia is granting export subsidies to a specific product contingent upon the incorporation of domestic raw material. These subsidies are scheduled under the Harmonized System Heading 19.05, HS number 1905.31 as follows: 55 million Subs and 600.000 tonnes.

Nevertheless, the Modalities Paper paragraph 9 of Annex 8 states that regarding incorporated products, “[b]ase and annual commitment levels shall be established for aggregate budgetary outlays in respect of subsidies on agricultural primary products incorporated in exported products (Annex 7 paragraph 1(f))”. Consequently, the Modalities Paper excludes Members from the obligation to comply with quantity commitments in those cases when export subsidies on incorporated products are granted.

In this way, the Panel during the assessment of Subsidia compliance with articles 3.3 and 8 of the AoA must focus strictly on Subsidia’s compliance with its budgetary outlays commitments. Consequently, it shall be concluded that considering the fact that the Respondent Member “has fully met its budgetary commitments”,⁶² then it is in compliance with articles 3.3 and 8 of the AoA.

- The correct to manner to schedule subsidies on incorporated products.

Finally, Subsidia will demonstrate that it has incorporated its commitments in the correct manner supported in two reasons. First, Subsidia has included quantities within its Schedule of Concessions in order preserve the opportunity to shift in the future the sort of export subsidy provided to the product. Second, the export subsidy on incorporated product is included within the heading 1905 and not as incorporated products, because this type of subsidy is only provided by the Member to a specific agricultural product.⁶³

62 Facts of the Case, para. 9.

63 This is the case of the European Communities that have established expressed commitments as “incorporated products”. See, WTO. http://www.wto.org/english/tratop_e/agric_e/ag_intro04_export_e.htm#reduction [accessed 30 december 2005].

First, it is important to clarify that according to articles 3 and 9 of the AoA there is a list of export subsidies that in case of being provided in respect to a specific product or group of products, they must be subject to reduction.⁶⁴ However, articles 3 and 9 of the AoA grants flexibility for a Member to decide what kind of subsidy they want to provide as long as they are in compliance with their reduction commitments.

Therefore, the fact that Subsidia has included quantities within its Schedule of Concessions does not obey to a wish of acquiring commitments beyond those required by the AoA, but to an aspiration to leave the door open for a future change in the type of the subsidy provided to the product.⁶⁵ In this way, while Subsidia is providing export subsidies to sweet biscuits under art. 9.1.f of the AoA, the provision of quantities reduction must remain ignored. Should Subsidia decides to change the sort of subsidy provided (i.e to any other listed in art 9.1 of the AoA), the quantities reductions provision will be triggered though. The latter explains why the application of Subsidia's quantities commitment is conditioned to the kind of subsidy bestowed. Furthermore, given the case that the subsidy currently provided by Subsidia to its sweet biscuits manufactures is a kind of subsidy under art. 9.1.f of the AoA, the commitment that matters is the budgetary outlays.

Second, other Members have scheduled its subsidies under art. 9.1.f of the AoA under the title "incorporated products". However, this is not the case of Subsidia as the export subsidy on incorporated product it is providing is

Consequently, the Council Regulation (EC) No 1784/2003 of 29 september 2003 on *the Common Organization of the Market in Cereal*, establishes export subsidies on incorporated products for more that 15 commodities with different Headings under the Harmonized System.

64 Art. 3.3 of the AoA states that "subject to the provisions of paragraphs 2(b) and 4 of Article 9, a Member shall not provide export subsidies listed in paragraph 1 of Article 9 in respect of the agricultural products or groups of products...". This stipulation supports the fact that member are allowed to change for the kind of subsidy without contravene the Agreement.

65 This interpretation is supported by the principle of *in dubio mitius*, according with "[i]f the meaning of a term is ambiguous, the meaning is to be preferred which is less onerous to the party assuming and obligation, or which interferes less with the territorial and personal supremacy of a party, or involves less general restrictions upon the parties". Didier Chambovey, "How the Expiry of the Peace Clause (Article 13 of the WTO Agreement on Agriculture) Might Alter Disciplines on Agricultural Subsidies in the WTO Framework", *Journal of World Trade*, 36(2) (2002), 305-352 (p. 310)

to a specific agricultural product (i.e sweet biscuits) and not to a group of products as happens with the other countries.⁶⁶

For the reasons expressed above, Subsidia is scheduling its commitment in the correct manner. Also, Subsidia is in compliance of its budgetary outlays commitments regarding export subsidies under art. 9.1.f, as it has been interpreted by the subsequent practice of the Members while considering the application of arts. 3.3 and 8 of the AoA.

2. Conclusion

Subsidia request to this Panel to rule that the Member is in compliance with Articles 3,8 and 9 of the AoA since it has fully met its export subsidies reduction commitments. Supporting the latter, it has been demonstrated to the Panel that the SBS is a dual nature measure, then, focusing on the export scenario, it was established that the payment made to sweet biscuits manufactures constitutes an export subsidy under article 9.1 (f) of the AoA. Finally, Subsidia proved that its reductions commitments were scheduled in the correct manner and were also fully respected regarding the issue of budgetary outlays.

III. Pork

Subsidia will establish that the PS Scheme is designed in accordance with article 6.5(a) of the AoA. The measure is a payment conditioned upon a production limiting program that has other concerns than trade. The scheme is not a domestic support or an export subsidy under the elements described in articles 6.1, 6.3 and 9 the AoA. Consequently, the PS is not inconsistent with the obligations contained on articles 3 and 8 of the same treaty.

1. The PS is in full compliance with Article 6.5 of the AoA

Subsidia will demonstrate that the PS can be regarded as a blue box measure. First, it will describe the design and structure of the measure. Second, it will

66 This is the case of the European Communities that have established expressed commitments as “incorporated products”. See, WTO. http://www.wto.org/english/tratop_e/agric_e/ag_intro04_export_e.htm#reduction, [accessed 28 december 2005]. Consequently, the Council Regulation (EC) No 1784/2003 of 29 september 2003 *on the Common Organization of the Market in Cereal*, establishes export subsidies on incorporated products for more that 15 commodities with different Headings under the Harmonized System.

determine how such design and structure is in full compliance with the purpose and objectives that inspire the AoA. Finally, it will address the nature of the payment promoting the concept of “multifunctionality of agriculture”.

1.1. Structure and Design of the Measure

In this section, Subsidia will establish that the payments under the blue box measures are not decoupled from production. Subsequently, it will address the fact that the nature of such payments are in conformity with WTO rulings.

The PS is designed as a measure that grants a payment to swine producer when they follow a plan laid out to each farm in order to reduce production from 9 million to 7 million.⁶⁷ The measure is structured upon a flexible payment. In this case, if a farmer exceeds the number of heads in a given year, he loses 50% of his support for that year and for the next one as well.⁶⁸ Therefore, a farmer loses the complete amount of its support payment. Accordingly, such a measure is executed during a two year period. Competia cannot claim that the payment is not conditioned to a production-limiting program. The facts are clear regarding that production will be limited since every farmer –except for one- is adequately implementing the plan.⁶⁹

This flexible payment has been analyzed by the US-Cotton Panel when it concluded that PFC – Production Flexibility Contracts- and DP –Deficiency Payments⁷⁰– are not subsidies which can be considered as Green Box Measures. The Panel stated:

There is little doubt that *in general* the “amount” of PFC and DP payments is not “related to, or based on, the type or volume of production ... undertaken by the producer in any year after the base period”. However, although there is no programme requirement to produce any particular product, where a producer in fact undertakes certain restricted types of production, such as fruits and vegetables, on some or all acres enrolled in the programme in a year after the base period, the amount of the

67 Facts of the Case, para. 12.

68 Facts of the Case, para. 13.

69 Facts of the Case, para 13.

70 For further analysis regarding production flexibility payments and Direct Payments see US-Cotton Panel Report. Pars. 7.2.12 – 7.2.2.6.

payment which that producer receives may be reduced. Where the farm or the producer meets certain special eligibility criteria, which essentially depend on a history of planting fruits or vegetables, there is a reduction in the amount of the payment, unless the region satisfies the special eligibility criteria, in which case there is no reduction. Where neither the farm nor the producer meets the special eligibility criteria, and the producer undertakes certain restricted types of production, such as fruits and vegetables, on some or all acres enrolled in the programme in a year after the base period, payments are revoked or there is a reduction in the amount of the payment by way of a penalty. It is with respect to these requirements, under which payments are eliminated or reduced, that Brazil claims that PFC and DP payments are not in conformity with the criterion in paragraph 6(b) of Annex 2 of the *Agreement on Agriculture* because the amount of such payments in any given year is related to, or based on, the type and volume of production undertaken by the producer in a year after the base period, and that therefore PFC and DP payments do not qualify for exemption from reduction commitments as decoupled income support.⁷¹

Paragraph 6 (b) of Annex 2 of the AoA determines that green box measures shall not be related or based upon the type or volume of production.⁷² Accordingly, the flexibility that such payments involve is not consistent with the Green Box measures.⁷³

In this case, the Panel did not address the nature of the payments in order to determine under what box they should be classified. Since these payments are conditioned upon types and volumes of production, Subsidia considers

71 Report of the Panel, *US-Cotton*, para 7.383.

72 Agreement on Agriculture, Annex 2, para. 6 (b).

“6. Decoupled income support

(b) The amount of such payments in any given year shall not be related to, or based on, the type or volume of production (including livestock units) undertaken by the producer in any year after the base period”.

73 Report of the Panel, *US-Cotton*, Para 7.387. “For the above reasons, the Panel concludes that PFC payments, DP payments, and the legislative and regulatory provisions that provide for the planting flexibility limitations in the DP programme, do not fully conform with paragraph 6(b) of Annex 2 of the *Agreement on Agriculture*”.

that such should be regarded as Blue Box Measures. When such payments condition the type of the products, they address the quantities, and by addressing the amounts they are production-limiting.

The PS has similar characteristics and shares the fundamental element of flexibility with the PFC and DP payments. Regarding these payments, the US-Cotton Panel determined:

“It is clear that the planting flexibility limitations at issue provide for the “amount” of PFC and DP “payments” to be reduced or eliminated by reference to the planting of fruit and vegetables (and wild rice) on base acres. Those producers who did not and do not plant fruit and vegetables (or wild rice) on their base acres did not and do not have the amount of their payments reduced. Those producers who did and do plant fruit and vegetables (and wild rice) on their base acres, whether in accordance with special eligibility criteria (with one exception) or not, did and do have the amount of their payments reduced”.⁷⁴

Two main conclusions arise from the rationale expressed by the Panel. First, payments based on a “flexibility requirement” cannot be considered as decoupled income support. Second, if such payments are not green box, and are conditioned by the type and volume of production –in this case by, these can be identified as subsidies within the blue box.

The PS Scheme is designed according to the rationale that explains the last two conclusions. It is a production-limiting program that conditions support to the farmers according to the number of heads they reduce within a year. However, the payment is flexible, since a 50% discount is applied during the first year, and the remaining support is reduced during the following one.

Interpreting the US-Cotton Panel statements, when a payment is not entirely decoupled from production it cannot be regarded as a green box. Accordingly, if a payment not entirely decoupled from production is scheduled in the blue box it has to be conditioned to a production-limiting program. The PS fits these conditions.

74 Report of the Panel, *US-Cotton*, para. 7.384.

1.2 The PS is in full compliance with the Object and Purpose of the AoA

The PS is in compliance with the object and purpose of the AoA since it is designed to effectively reduce production.

The objective of the AoA is to establish a fair and market oriented agricultural trade policy.⁷⁵ Subsidia recognizes that its measures must be in accordance with such a principle and therefore a blue box subsidy cannot be designed to encourage overproduction and affect world market prices.⁷⁶ In this case –as it has been mentioned before-, the payment is granted once the farmer reduces effectively the number of heads according to the plan laid out for each farm. A complex calculation system exists in order to ensure that a 9 to 7 million reduction in the swine production will take place. It is important to point out that neither the AoA nor any other WTO treaty conditions the terms of the production-limiting program, and therefore the PS falls within the elements described in article 6.5 of the same treaty.

The PS is not designed to ensure a stable yearly income to swine producers. Conversely, it has been structured to assure that a reduction in the swine production will reflect in sustainable environmental protection.

1.3 Multifunctionality of Agriculture

The concept of Multifunctionality is relevant in this case. It has been understood as “any unpriced spillover benefits that are additional to the provision of food and fibre. Claimed benefits range from environmental values, rural amenities, cultural values, rural employment and rural development”.⁷⁷

75 Agreement on Agriculture. Preamble.

76 Scholar Carmen González has stated “Finally, the inequity with respect to “amber box” subsidies is compounded by the fact that the Agreement exempts from its subsidy reduction obligations many of the subsidies traditionally utilized by developed countries. The so—alled “blue box” and “green box” exemptions to the domestic support provisions impinge on food security in developing countries by encouraging overproduction in developed countries, which depresses world prices and creates disincentives to domestic production”. Carmen G. Gonzalez, “Institutionalizing Inequality: the WTO Agreement on Agriculture, Food Security, and Developing Countries”, *Columbia Journal of Environmental Law*, 27 (2002), 433-490 (p. 484).

77 Bhala, Raj. *International Trade Law*, p. 721.

It is important to understand that Subsidia's purpose in reducing production is to protect the environment. The one producer that has not reduced the number of heads is in jail for violating laws of swine-related pollution of the ground water.⁷⁸ Therefore, Subsidian laws have the highest concerns for sustainable development. Law Number 345 Section 40 provides a payment with the purpose of enhancing spillover benefits in the environment. This is the non-trade concerns that must be addressed in order to understand that the payment in the scheme is flexible.

In order to guarantee conditions like sustainable development, it is particularly important to include flexibility within the granting of the payments. The measure's progressive discount provides farmers with the resources to address such environmental concerns. There is no sense in withdrawing the complete amount of the payment within one year to a farmer that wasn't able to cut down production, so that the next one he wouldn't have the resources to fulfill the conditions of the program. Consequently, the idea of the discount is to allow farmers to remain within the possibilities to comply with the reduction plan for the next year.

Article 31.3.(c) of the Vienna Convention establishes that any relevant rules of international law applicable in the relationships between the parties shall be interpreted taken into account the context treaties.⁷⁹ In order to understand the relationship between the AoA and the environment other instruments must be observed.

The environment is protected by international law. The Rio Declaration on Environment and Development of 1992 is a relevant standard in order to interpret the obligations that Subsidia must comply with.⁸⁰ This instrument

78 Facts of the Case, para. 13.

79 Vienna Convention on The Law of Treaties. Article 31.3.c. There shall be taken into account, together with the context: (c) any relevant rules of international law applicable in the relations between the parties.

80 Scholar D.J. Harris has classified the Rio Declaration of Environment and Development of June 1992 as an example of soft law provisions. Regarding the concept soft law the author expressed "while it may be paradoxical and confusing to call something "law" when it is not law, the concept is nonetheless useful to describe instruments that clearly have an impact on international relations and that may later harden into custom or become the basis of a treaty. And as Jennings has stated "recommendations may not make law, but you would hesitate to advise a government that it may, therefore, ignore them, even in a legal argument ." Seidl-Hohenveldern suggests that the main value of international "soft law", which is very important in the field of international law, is a device to "overcome a deadlock in relations between

establishes that States should reduce or eliminate unsustainable patterns of production in order to achieve sustainable development.⁸¹ Therefore, a blue box measure is justified in this case in order to fulfill other kinds of international obligations.

Subsidia acknowledges that a conflict between free trade and environmental protection arises. Accordingly, there are two public policy choices that must be analyzed. Subsidia found that the AoA contained the necessary mechanisms and provisions in order to solve the issue. Therefore, the problem was addressed by correctly executing the provisions contained in article 6.5 of this treaty –establishing an effective production-limiting programme that could strengthen the country’s sustainable development. Consequently, free trade was not harmed or ignored in any way. The WTO relevant covered agreement –the AoA in this case- was applied and Principle 12 from the Rio Declaration was not overlooked.⁸²

The AoA is not a covered agreement that must be applied without considering other international instruments. In this case, soft law provisions –such as the Rio Declaration– serve as a mean to interpret the treaty according to article 31.3.c of the Vienna Convention.

states pursuing conflicting ideological or economical aims” (emphasis added). D.J. Harris, *Cases and Materials on International Law*, 5th edn (London Sweet and Maxwell 1998), p. 65.

- 81 Rio Declaration on Environment and Development of June 1992. Principle 2. States have, in accordance with the Charter of the United Nations and the principles of international law, the sovereign right to exploit their own resources pursuant to their own environmental and developmental policies, and the responsibility to ensure that activities within their jurisdiction or control do not cause damage to the environment of other States or of areas beyond the limits of national jurisdiction.

Principle 8. To achieve sustainable development and a higher quality of life for all people, States should reduce and eliminate unsustainable patterns of production and consumption and promote appropriate demographic policies.

- 82 Principle 12 States should cooperate to promote a supportive and open international economic system that would lead to economic growth and sustainable development in all countries, to better address the problems of environmental degradation. Trade policy measures for environmental purposes should not constitute a means of arbitrary or unjustifiable discrimination or a disguised restriction on international trade. Unilateral actions to deal with environmental challenges outside the jurisdiction of the importing country should be avoided. Environmental measures addressing transboundary or global environmental problems should, as far as possible, be based on an international consensus.

Subsidia designed an effective measure within the terms of article 6.5 a., such a measure complies with the objectives and purpose of that agreement. Finally, it was structured to address environmental concerns, which are protected by international law as well.

1.4 Conclusion

Subsidia did not violate articles 6.5a, 6.1, 6.3 and 3.2 of the AoA. The PS can be regarded as a Blue Box subsidy, and therefore is not subject to any reduction commitments. If the Panel found that the PS were to be inconsistent with the obligations described in article 6.5a of the AoA, these articles would also be violated. Nonetheless, the PS is not under any circumstance an export subsidy described within the terms of article 9 of the mentioned treaty.

2. The Payments granted within the PS are not Export Subsidies

Subsidia did not violate articles 9,3.3, and 8 of the AoA. The payment within the PS is not an export subsidy. The measure is a domestic support since it is not granted upon swine export performance. Moreover, the subsidy has no spill over effect since it is a WTO-inconsistent domestic support. Accordingly, the measure was not subject to reduction commitments as an export subsidy.

Under the assumption that the Panel rules that the PS is not a blue box subsidy, it would be a WTO-inconsistent domestic support. The payment is not conditional upon export, and it is not designed to create any advantage on exports. In this case, as The Canada-Dairy AB suggested, the only way a domestic support can be regarded as an export subsidy is through a spill over effect. The Panel stated:

“It is possible that the economic effects of WTO-consistent domestic support in favour of producers may “spill over” to provide certain benefits to export production, especially as many agricultural products result from a single line of production that does not distinguish whether the production is destined for consumption in the domestic or export market”.⁸³

83 Appellate Body Report, *Canada - Measures Affecting the Importation of Milk and the Exportation of Dairy Products*- Recourse to Article 21.5 of the DSU. WT/DS103/AB/RW WT/DS113/AB/RW, 3 december 2001, para. 89.

The Canada-Dairy AB analyzed this issue within the scope of WTO-consistent domestic support. The PS would be an inconsistent domestic support if it is found not to be a blue box measure, Therefore, no spill over effect is created by a payment with such a characteristic.

Domestic support measures and export subsidies hold different standards and, in this case, there is no basis to consider the subsidy as the one defined in article 9 of the AoA. Regarding the differences between export subsidies and WTO-consistent domestic support, the AB established:

“We believe that it would erode the distinction between the domestic support and export subsidies disciplines of the *Agreement on Agriculture* if WTO-consistent domestic support measures were automatically characterized as export subsidies because they produced spill-over economic benefits for export production. Indeed, this is another reason why we do not agree with the Panel that sales of CEM at any price below the administered domestic price for milk can be regarded as “payments” under Article 9.1(c) of the *Agreement on Agriculture*. Such a basis for comparison would tend to collapse the distinction between these two different disciplines”.⁸⁴

The issue in this case is to establish if WTO-inconsistent domestic support can be regarded as an export subsidy. There are no arguments to hold this position. In fact, if this Panel were to consider such a premise, the distinction between export subsidies and domestic support would be eroded as well. WTO-inconsistent domestic support would be a domestic support anyway, and even if the payments produce economic advantages under export production, there would not be an export subsidy under the AB rationale.

Regarding the reasons stated above, Subsidia did not violate articles 9, 3.3, and 8 since the payments are not export subsidies and should not be subject to reduction commitments.

Conclusion

Subsidia request the Panel to dismiss the claims raised by Competia regarding the violation of articles 3, 6, and 9 of the AoA and Part III of the SCM.

84 Appellate Body Report, *Canada-Dairy (Article 21.5)*, para. 90.

VII. CONCLUSIONS

1. The authors believe that the solution regarding the possibility of challenging agricultural export subsidies under SCM provisions can be found by giving an effective interpretation to the three relevant WTO provisions referring to this matter.

First, it is clear that if members agreed to exempt agricultural export subsidies from being challenged under SCM provisions for a certain period of time (Article 13 of the AoA), it was because they believed that, absent that exemption, agricultural export subsidies could be challenged using Part III of the SCM Agreement. On the other hand, it is clear that all export subsidies have trade-distorting effects, and that Members did not allow the granting of payments that would always result in adverse effects to the interests of other Members, and therefore, that would always be challengeable under Part III of the SCM.

To the authors the solution is to take a middle position acknowledging that there are two types of trade distorting effects. First those trade-distorting effects accepted by WTO Members that do not reach the sufficient level of distortion to cause adverse effects in the sense of Part III of the SCM. To these trade-distorting effects Part III the SCM cannot be applied. Second, those trade-distorting effects that reaches a level of distortion sufficient to cause adverse effects to the interests of other Members. These kinds of subsidies may be challenged under SCM provisions, even though they are not prohibited under the AoA. This interpretation encloses the cumulative application of WTO Agreements, and the principle of effective interpretation.

2. The authors suggest that a solution to the problem of disguising export subsidies behind domestic support schemes can be found on the interpretation made by the EC-Sugar Panel of Article 9.1(c) of the AoA. As stated by the Panel, if the term “payments

on the export” is interpreted in a broader sense that prevails over the classical definition of export subsidies as payments contingent upon export performance, Members will find a limitation to promote exports under domestic support schemes. However, the Appellate Body has neither upheld nor rejected this advanced interpretation proposed by the EC-Sugar Panel, what leaves the solution in stand by, waiting for a future dispute on export subsidies.

3. Finally, the authors consider that there is a possibility to set a limit to the granting of subsidies provided under blue box schemes if the term “direct payment under production limiting programmes” is interpreted in consistency with the preamble of the AoA. Accordingly, the analysis of the legality of a Blue box measure under the AoA should not be reduced to the verification of the existence of a (i) direct payment under a (ii) production limiting programme, but, it must also include the analysis of its trade distorting effects in order to be considered apt to be excluded from the domestic support reduction commitments required by the Agreement.

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