

EUROPEAN ECONOMIC COMMUNITY - SUBSIDIES ON EXPORT OF WHEAT FLOUR

*Report of the Panel  
(SCM/42)*

I. Introduction

1. In pursuance of the decision of the Committee on Subsidies and Countervailing Measures taken at its meeting of 14 December 1981, concerning the establishment of a panel to examine the complaint by the United States (SCM/Spec/6), the Chairman of the Committee, after securing the agreement of the Signatories concerned set, on 22 January 1982, the following terms of reference and the composition of the panel:

A. Terms of Reference

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

B. Composition

Chairman: H.E. Ambassador Fumihiko Suzuki, Permanent mission of Japan, Geneva

Members: Mr. D.E. Hobson, First Secretary, Permanent Mission of Canada, Geneva  
Mr. R. Lempen, Office fédéral des affaires économiques extérieures, Berne

2. The Panel met with the Parties to the dispute on 24 February, 11 March and 6 April 1982.

II. Main arguments

2.1 In presenting its complaint to the Committee, the United States delegation claimed that EEC subsidies on the export of wheat flour were:

(a) applied in a manner inconsistent with Article 10:1 of the Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade (hereinafter referred to as "the Code") in that they have resulted in the EEC having more than an equitable share of the world export trade in wheat flour,

(b) applied in a manner which results in prices materially below those of other suppliers to the same market in violation of Article 10:3 of the Code,

(c) causing nullification or impairment of benefits accruing to the United States under the General Agreement and serious prejudice to the interests of the United States in terms of Article 8 of the Code.

2.2 The Panel heard arguments of the parties with respect to the various points of the complaint as listed in paragraph 2.1 above. A summary of the arguments presented by the parties on each of these points is set out below (paragraphs 2.5 to 2.38).

2.3 In addition to the points, in his presentation to the Panel, referred to in para 2.1, the US

representative argued that the EEC export subsidies on wheat flour are prima facie contrary to the obligations of Article 9 of the Code, since, in the US view, wheat flour is a processed product, not a primary product within the meaning of the Code.

2.4 The EEC representative argued that, since the U.S. representative had not referred to Article 9 in raising the matter in the Committee, the question of whether Article 9 applied to wheat flour did not fall within the terms of reference of the panel.

A. EEC subsidies on the export of wheat flour are applied in a manner inconsistent with Article 10:1 of the Code in that they have resulted in the EEC having more than an equitable share of the world export trade in wheat flour

#### United States arguments

2.5 The representative of the United States said that as neither the Code nor the GATT provided, and previous panels had not established, a definition for the term "more than an equitable share", the Panel must interpret the phrase in light of the facts of this case taking into account the guidance in Article 10:2(a) of the Code which stated that "more than an equitable share of world export trade" should include any case in which the effect of an export subsidy granted by a Signatory was to displace the exports of another Signatory. He believed that the EEC share of world commercial export trade in wheat flour resulting from the operation of its export subsidy system was inequitable, and that EEC exports had displaced the exports of the US and other Signatories.

2.6 In this relation, he recalled that this was not the first time world export trade in wheat flour has been examined by a GATT panel. In the 1958 Australian complaint regarding French subsidies on wheat and wheat flour, a panel had determined that France had obtained more than an equitable share on the world wheat flour market through subsidization (BISD 7th Supplement, page 52).

2.7 The representative of the United States said that since the assessment of "inequitable share" should be made by taking into account the share held during a previous representative period, it was necessary to first determine a period applicable in this case. As Article 10:2(c) provided that "a previous representative period shall normally be the three most recent calendar years in which normal market conditions existed" he argued that the use of the words "normally" and "normal" market conditions provided the Panel with considerable flexibility in choosing a representative period. Although no definition had been given to the term "normal market conditions", past GATT practice had taken "special factors" into account in allowing the selection of a period other than the three most recent years as "representative" and the Code permitted the continuation of this practice.

2.8 He further said that the three most recent calendar years could not be used as the representative period in this case since, given the distortion of trade patterns resulting from the heavy use of export subsidies by the EEC, it did not constitute a period during which "normal market conditions existed". There was ample GATT precedent for selecting a period when subsidization was not unduly affecting the market shares. During the 1955 Review Session it was agreed that in determining what is an equitable share of world trade, the CONTRACTING PARTIES should not lose sight of "the fact that export subsidies in existence during the selected representative period may have influenced the share of the trade obtained by the various exporting countries". (GATT, BISD 3rd Supplement, paragraph 19, page 226). Then, in 1960, the CONTRACTING PARTIES adopted a Panel Report which dealt with notification of subsidies, in which it was agreed that an analysis of the effect of a subsidy should include statistics "... for a previous representative year, which where possible and meaningful, should be the latest period preceding the introduction of the subsidy or preceding the last major change in the subsidy." (GATT, BISD 9th Supplement, Annex II(b) (ii), page 194).

2.9 He considered that there was no question that the EEC export subsidy programme had influenced its share of world flour trade. Given the high support prices for wheat in the EEC, export sales of flour from domestic wheat could not have occurred in the absence of subsidies. Thus, it was necessary to examine a period which preceded the adoption of the EEC's subsidy system in order to assure that the trade distorting effect which the EEC system has already had on world markets was minimized as a factor in judging "equitable share". Accordingly, the United States had used as a reference period the three marketing years preceding the establishment of the CAP in 1962. Although this required the Panel to look back 20 years to make a comparison, it was necessary to do so to have a true picture of the world wheat flour market. In addition to comparing an early three-year period to the most recent three-year period, he also requested the Panel to examine the entire period from 1959/60 to 1980/81 in order to examine the trends in the market. He noted that there was considerable GATT precedent for considering an entire period. In the above-mentioned dispute between France and Australia, the Panel had considered the entire interwar and postwar periods, spanning more than 20 years, in determining that the French share of world export trade, particularly, in wheat flour, had been more than equitable<sup>1</sup>. In the 1979 sugar dispute between the EEC and Australia, the Panel had considered various alternative periods and made a set of comparisons. In that case, the EEC itself had argued for a five-year period, claiming that the years chosen should reflect "normal-market conditions"<sup>2</sup>. Then, in the 1980 sugar dispute between the EEC and Brazil, the Panel had selected multiple periods for its examination<sup>3</sup>.

2.10 The United States pointed out that between the reference period and the most recent period, the EEC had increased its share dramatically from 29 to 75 per cent. (Table I and II).

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<sup>1</sup>GATT, "French Assistance to Exports of Wheat and Wheat Flour", BISD 7th Supplement, page 52 (1959), L/924.

<sup>2</sup>GATT, "European Communities - Refunds on Exports of Sugar, Complaint by Australia", L/4833, 25 October 1979.

<sup>3</sup>GATT, "European Communities - Refunds on Exports of Sugar, Complaint by Brazil", L/5011, 7 October 1980.

Table I  
 RELATIVE SHARES OF THE WORLD COMMERCIAL  
 FLOUR MARKET  
 (Volume in 1,000 metric tons wheat equivalent)

	<u>Reference Period</u> (1959/60-61/62)		<u>Most Recent 3-Year Period</u> (1978/79-80/81)	
	<u>Average Volume</u>	<u>Average Share</u>	<u>Average Volume</u>	<u>Average Share</u>
US	864	25 %	437	9 %
EEC	1,013	29 %	3,531 *	75 %
Australia	715	20 %	78	2 %
Canada	881	25 %	546	11 %
Other	40	1 %	152	3 %
<u>TOTAL</u>	<u>3,514</u>		<u>4,764</u>	

\*EEC food aid shipments were not separate from commercial transactions in data submitted to the IWC by the EEC for 1977/78, 1978/79, and 1979/80, although the EEC in 1980 began to separate commercial and special transactions in its reporting for 1980/81. Based on EEC wheat flour aid levels in the previous 6 years, we have estimated such shipments at 10.8 per cent of total exports and deducted these amounts in estimating EEC commercial shipments for 1978/79-1979/80.

Data for 1980/81 are preliminary IWC statistics, just received in November, 1981.

Source: cf. Table II.

TABLE II

WHEAT FLOUR: WORLD COMMERCIAL EXPORTS  
CROP YEARS 1959/60-1980/81  
(1,000 Metric Tons Wheat Equivalent)  
(table submitted by the United States)

	<u>59/60</u>	<u>60/61</u>	<u>61/62</u>	<u>62/63</u>	<u>63/64</u>	<u>64/65</u>	<u>65/66</u>	<u>66/67</u>	<u>67/68</u>	<u>68/69</u>	<u>69/70</u>
Australia .....	744	747	654	577	871	702	486	527	483	377	310
Canada .....	964	856	824	697	1,501	772	988	678	526	528	626
U.S. ....	1,028	826	739	527	545	493	505	853	360	341	259
EEC <sup>1</sup> .....	947	879	1,214	991	1,416	1,531	1,438	1,754	1,232	1,239	1,717
Other .....	94	14	13	89	126	182	147	280	894	402	481
Total .....	3,777	3,322	3,443	2,881	4,459	3,680	3,564	4,092	3,495	2,887	3,393
-- Market Share -- (%)											
	<u>59/60</u>	<u>60/61</u>	<u>61/62</u>	<u>62/63</u>	<u>63/64</u>	<u>64/65</u>	<u>65/66</u>	<u>66/67</u>	<u>67/68</u>	<u>68/69</u>	<u>69/70</u>
Australia ....	20	22	19	20	20	19	14	13	14	13	9
Canada .....	26	26	24	24	34	21	28	17	15	18	18
U.S. ....	27	25	21	18	12	13	14	21	10	12	8
EEC <sup>1</sup> .....	25	26	35	34	32	42	40	43	35	43	51
Other .....	2	*	*	3	3	5	4	7	26	14	14

<sup>1</sup> EEC-6 until 1973; EEC-9 thereafter.

\* Less than one per cent.

Source: IWC, Annual Record of Operations.

WHEAT FLOUR: WORLD COMMERCIAL EXPORTS  
CROP YEARS 1959/60-1980/81  
(1,000 Metric Tons Wheat Equivalent)

	<u>70/71</u>	<u>71/72</u>	<u>72/73</u>	<u>73/74</u>	<u>74/75</u>	<u>75/76</u>	<u>76/77</u>	<u>77/78</u> <sup>2</sup>	<u>78/79</u> <sup>2</sup>	<u>79/80</u> <sup>2</sup>	<u>80/81</u> <sup>3</sup>
Australia .....	299	241	167	160	265	280	273	108	81	76	78
Canada .....	595	506	509	386	480	509	54	513	608	569	462
U.S. ....	265	252	313	282	357	493	335	505	440	466	404
EEC <sup>1</sup> .....	1,496	2,111	2,382	2,356	2,204	2,653	2,095	2,761	2,926	3,679	4,047
Other .....	392	181	339	179	219	166	39	72	117	245	93
Total .....	3,047	3,291	3,710	3,363	3,525	4,101	2,796	3,959	4,172	5,035	5,084
-- Market Share -- (%)											
Australia .....	10	7	5	5	8	7	10	3	2	2	2
Canada .....	20	15	14	11	14	12	2	13	15	11	9
U.S. ....	9	8	8	8	10	12	12	13	11	9	9
EEC <sup>1</sup> .....	49	64	64	70	63	65	75	70	70	73	80
Other .....	13	5	9	5	6	4	1	2	3	5	2

<sup>1</sup> EEC-6 until 1973; EEC-9 thereafter

<sup>2</sup> EEC food aid shipments were not separated from commercial transactions in data submitted to the IWC by the EEC for 1977/78, 1978/79 or 1979/80, but such transactions were reported separately again for 1980/81. Therefore, based on EEC wheat flour aid levels in the 6 years prior to 1977/78, we have estimated special transactions at 10.8 per cent of total flour exports and have deducted these amounts in estimating EEC commercial shipments for 1977/78, 1978/79 and 1979/80.

<sup>3</sup> Adjusted for discrepancies in IWC data.

Source: IWC, Annual Record of Operations.

In comparison, the market share and volume of all other major exporters had been marked by an equally dramatic decline. The average US share had fallen from 25 per cent to 9 per cent and its average volume had declined by nearly 50 per cent. Australia's average share had dropped from 20 per cent to 2 per cent and Canada's average share from 25 per cent to 11 per cent. The enormous increase in the EEC's wheat flour exports, accompanied by the commensurate decrease in the market share of all other major suppliers indicated, by itself, the acquisition of "more than an equitable share" of world export trade. The US representative considered it appropriate to focus on commercial wheat flour transactions, as in Tables I and II, rather than also including special transactions, such as PL 480 or food aid programmes of the EEC and other countries. PL 480 transactions are virtually entirely food aid, either donations or sales on highly concessional terms. PL 480 shipments are typically granted on the condition that Usual Marketing Requirements for commercial imports be met from whatever source may be selected by the PL 480 recipient. There are various rules, particularly in the FAO, designed to protect commercial markets from adverse effects of special transactions. The US representative emphasized, however, that even if commercial and special transaction were considered together, as in Table III, the EEC share must still be considered more than equitable, having risen from an average of 18 per cent in the three year period 1959/60-1961/62 to 62 per cent during 1978/79-1980/81. This dramatic rise had occurred to the detriment of the United States and other exporters. He argued that the dramatic shift in market shares to the advantage of the EEC, and to the disadvantage of all other suppliers, had occurred because the EEC's subsidized wheat flour exports had displaced the exports of other suppliers in violation of Article 10:1, as interpreted by Article 10:2(a). He considered it self-evident that, in a market divided among four suppliers, the dramatic expansion of one supplier's share, particularly when the market was not expanding, must displace the exports of other suppliers. This displacement resulted from export subsidies which made price undercutting possible.

2.11 He further considered that in the case of wheat flour, it was particularly appropriate to focus on total world commercial trade, because the market structure for this product was characterized by a large number of importing countries, many of which purchased relatively small quantities of flour. In addition, there was a great deal of volatility in particular markets, reflecting changes in milling capacity, in income and demand, and in domestic food production. Moreover, essentially all types of flour and specifications demanded by individual countries could be supplied by the technologically advanced and highly diversified US industry if it were able to compete in those markets. Thus, EEC export subsidies hampered US export possibilities not just in some but in the majority of specific markets. He emphasized that a finding of displacement in specific markets was not required in determining that the EEC had used export subsidies to gain more than an equitable share of the world market. However, a comparison of flour exports to specific national markets lent further support to the US contention that EEC exports had displaced or pre-empted those of the United States. The seventeen markets shown in Table IV comprised 57 per cent of world wheat flour trade in 1980/81.

TABLE III

COMMERCIAL AND SPECIAL TRANSACTION  
WHEAT FLOUR EXPORTS BY SOURCE  
CROP YEARS 1959/60 - 1980/81  
(1,000 Metric Tons Wheat Equivalent)  
(Table submitted by the United States)

	<u>59/60</u>	<u>60/61</u>	<u>61/62</u>	<u>62/63</u>	<u>63/64</u>	<u>64/65</u>	<u>65/66</u>	<u>66/67</u>	<u>67/68</u>	<u>68/69</u>	<u>69/70</u>
Australia ....	744	758	654	586	871	716	486	551	497	475	429
Canada .....	1,032	967	870	132	1,528	800	1,082	819	593	626	783
U.S.....	2,382	2,907	2,946	2,601	2,701	2,309	2,376	2,035	1,689	2,104	1,402
EEC <sup>1</sup> .....	947	880	1,218	991	1,416	1,531	1,449	1,754	1,232	1,239	1,750
Other.....	94	47	13	89	251	531	508	779	1,494	459	1,136
Total .....	5,198	5,559	5,701	4,999	6,767	5,887	5,901	5,938	5,505	4,903	5,500
-- Market Share --											
(%)											
Australia ....	14	14	11	12	13	12	8	9	9	10	8
Canada .....	20	17	15	15	23	14	18	14	11	13	14
U.S.....	46	52	52	52	40	39	40	34	31	43	25
EEC <sup>1</sup> .....	18	16	21	20	21	26	24	30	22	25	32
Other.....	2	1	*	1	4	9	9	13	27	9	21

<sup>1</sup>EEC-6 until 1973; EEC-9 thereafter.

<sup>2</sup>Adjusted for discrepancies in IWC data and for donations to India.

\*Less than 1 per cent.

Source: IWC, Annual Record of Operations.

COMMERCIAL AND SPECIAL TRANSACTION  
WHEAT FLOUR EXPORTS BY SOURCE  
CROP YEARS 1959/69-1980/81  
(1,000 Metric Tons Wheat Equivalent)

	<u>70/71</u>	<u>71/72</u>	<u>72/73</u>	<u>73/74</u>	<u>74/75</u>	<u>75/76</u>	<u>76/77</u>	<u>77/78</u>	<u>78/79</u>	<u>79/80</u>	<u>80/81</u> <sup>2</sup>
Australia ....	414	272	215	200	312	299	308	160	114	97	136
Canada.....	764	653	599	458	551	883	324	783	818	693	547
U.S.....	1,670	1,504	1,337	816	936	950	1,645	1,539	1,462	1,487	1,394
EEC <sup>1</sup> .....	2,008	2,431	2,720	2,572	2,456	2,906	2,400	3,096	3,280	4,125	4,404
Other.....	570	245	378	238	296	302	148	157	115	297	153
Total .....	5,426	5,105	5,249	4,284	4,551	5,340	4,825	5,735	5,789	6,699	6,634

-- Market Share --  
(%)

Australia ....	8	5	4	5	7	6	6	3	2	1	2
Canada.....	14	13	11	11	12	17	7	14	14	10	8
U.S.....	31	29	25	19	21	18	34	27	25	22	21
EEC <sup>1</sup> .....	37	48	52	60	54	54	50	54	57	62	66
Other.....	11	5	7	6	7	6	3	3	2	4	2

<sup>1</sup> EEC-6 until 1973; EEC-9 thereafter.

<sup>2</sup> Adjusted for discrepancies in IWC data and for donations to India.

\* Less than 1 per cent.

Source: IWC, Annual Record of Operations.

TABLE IV  
 U.S. and EEC Flour Exports  
 to Specific Markets  
 (1,000 Metric Tons Wheat Equivalent)  
 (Table submitted by the United States)

	<u>Reference Period</u> <u>1959/60 - 61162</u>		<u>Most Recent 3-Year Period</u> <u>1978/79 - 80181</u>
<u>A. Markets Where U.S. Share Has Declined</u>			
	<u>Vol.</u>	<u>Market Share</u>	
			<u>Vol.</u> <u>Market Share</u>
			<u>Barbados</u>
U.S.	6.5	43%	0.0      0%
EEC	3.6	24%	5.1      63%
<u>Other</u>	<u>4.9</u>	<u>33%</u>	<u>3.0</u> <u>37%</u>
TOTAL	15.0	100%	8.0      100%
			<u>Cameroon</u>
U.S.	1.3	100%	0.0      0%
EEC	0.0	0%	54.0      100%
<u>Other</u>	<u>0.0</u>	<u>0%</u>	<u>0.0</u> <u>0%</u>
TOTAL	1.3		54.0
			<u>Chile</u>
U.S.	34.8	70%	0.0      0%
EEC	13.1	26%	22.2      100%
<u>Other</u>	<u>1.6</u>	<u>4%</u>	<u>0.0</u> <u>0%</u>
TOTAL	49.5		22.2
			<u>Israel</u>
U.S.	0.3	100%	0.1      1%
EEC	0.0	0%	26.0      99%
<u>Other</u>	<u>0.0</u>	<u>0%</u>	<u>0.0</u> <u>0%</u>
TOTAL	0.3		26.1
			<u>Jamaica</u>
U.S.	29.6	28%	14.3      19%
EEC	30.5	29%	55.4      74%
<u>Other</u>	<u>45.8</u>	<u>43%</u>	<u>5.5</u> <u>7%</u>
TOTAL	105.9		75.2
			<u>Jordan</u>
U.S.	16.3	26%	0.1      0%
EEC	45.7	74%	33.8      100%
<u>Other</u>	<u>0.0</u>	<u>0%</u>	<u>0.0</u> <u>0%</u>
TOTAL	62.0		33.9

Lebanon

U.S.	42.9	100%	0.3	2%
EEC	0.0	0%	12.7	98%
<u>Other</u>	<u>0.0</u>	<u>0%</u>	<u>0.0</u>	<u>0%</u>
TOTAL	42.9		13.0	

Nigeria

U.S.	41.7	55%	5.6	6%
EEC	1.6	0%	76.3	94%
<u>Other</u>	<u>32.7</u>	<u>45%</u>	<u>0.0</u>	<u>0%</u>
TOTAL	76.0	100%	81.9	100%

Philippines

U.S.	53.9	40%	0.5	4%
EEC	0.9	0%	4.7	35%
<u>Other</u>	<u>80.7</u>	<u>60%</u>	<u>8.3</u>	<u>61%</u>
TOTAL	135.5		13.5	

Saudia Arabia

U.S.	77.8	92%	204.2	38%
EEC	1.8	2%	322.3	61%
<u>Other</u>	<u>8.2</u>	<u>6%</u>	<u>4.6</u>	<u>1%</u>
TOTAL	87.8		531.1	

Sierra Leone

U.S.	2.8	19%	0.0	0%
EEC	0.0	0%	21.4	100%
<u>Other</u>	<u>11.7</u>	<u>81%</u>	<u>0.0</u>	<u>0%</u>
TOTAL	14.5		21.4	

Trinidad-Tobago

U.S.	33.0	42%	0.0	0%
EEC	4.7	6%	2.1	70%
<u>Other</u>	<u>41.3</u>	<u>52%</u>	<u>0.9</u>	<u>30%</u>
TOTAL	79.0		3.0	

Zaire

U.S.	6.4	30%	1.4	30%
EEC	1.9	9%	2.5	66%
<u>Other</u>	<u>13.0</u>	<u>61%</u>	<u>0.0</u>	<u>0%</u>
TOTAL	21.3		3.9	

B. Markets Where US Has Been Virtually Excluded

Egypt

U.S.	0.1	0%	117.3	11%
EEC	35.2	56%	988.0	89%
<u>Other</u>	<u>27.3</u>	<u>44%</u>	<u>1.0</u>	<u>0%</u>
TOTAL	62.6		1,106	



<u>Sri Lanka</u>				
U.S.	0.0	0%	1.4	0.5%
EEC	7.9	100%	314.3	99.0%
<u>Other</u>	<u>0.0</u>	<u>0%</u>	<u>1.1</u>	<u>0.5%</u>
TOTAL	7.9		316.8	
<u>Syria</u>				
U.S.	0.0	0%	7.0	2%
EEC	0.0	0%	354.2	97%
<u>Other</u>	<u>2.4</u>	<u>100%</u>	<u>2.1</u>	<u>1%</u>
TOTAL	2.4		363.3	
<u>Yemen</u>				
U.S.	0.0	0%	0.0	0%
EEC	2.9	100%	101.6	100%
<u>Other</u>	<u>0.0</u>	<u>0%</u>	<u>0.0</u>	<u>0%</u>
TOTAL	2.9		101.6	

SOURCE: IWC, Annual Record of Operations.

2.12 According to the representative of the United States Part A of Table III demonstrated displacement in a number of specific national markets of varying sizes and growth patterns. In each of these markets, the US had been commercially active in the early 1960's, prior to the CAP. By comparison, the US share of the market in the most recent 3-year period had declined sharply in nearly all of these countries. In several countries (Cameroon, Chile, Jordan, Sierra Leone, Trinidad and Tobago), the US had been completely displaced from the market. The largest market where the US share had declined was Saudi Arabia. Saudi Arabia had been one of the largest and fastest growing wheat flour markets, with demand expanding more than sevenfold over the past 20 years. During the early 1960's, the United States had supplied 92 per cent of Saudi flour import needs while the EEC had accounted for only 2 per cent. However, during the most recent 3-year period, the US share had fallen to 38 per cent while the EEC share had risen to 61 per cent.

2.13 Part B of Table IV showed the strong growth that had occurred in a number of key markets over the 20-year period. Imports by Egypt, Sri Lanka, Syria and Yemen had accounted for about 40 per cent of total world commercial flour imports in recent years. However, the US, competing with artificially low EEC prices, had been able to participate in this expansion only to a minimal extent, and, in the case of Sri Lanka, Syria and Yemen, the US had been excluded almost entirely.

#### EEC counter-arguments

2.14 The representative of the EEC said that the crucial problem emerging from the United States complaint was that of the exclusion of exports on special terms. It was clear from Table I, that the United States was referring solely to what was termed the commercial market, in other words concessional deliveries were not taken into account. However it was fundamental for defining the nature of commitments under the Code to know whether the United States was justified in interpreting the expression "world export trade" as meaning "commercial exports" and by what criteria the latter were determined. In this connection he pointed out that there were no uniform and unanimously recognized criteria for determining whether or not deliveries were commercial. Available world

statistics (those for example of the International Wheat Council and FAO) were based on statements made by the countries concerned which the organizations simply recorded; in other words, any differentiation they might make between the two types of trade was based on each country's own criteria, which would vary greatly. It was impossible, therefore, to compare figures based on these different criteria. The only objective comparison could be aggregate figures "commercial" plus "concessional". The United States practised an agricultural surplus disposal policy in the form of sales under the Agricultural Trade Development and Assistance Act, commonly known as Public Law 480 or PL 480. For the needs of the present case, the United States considered that PL 480 constituted food aid and should not be counted as part of "world trade", on the grounds that it operated in favour of less-developed countries and on conditions that were indeed very advantageous. PL 480 was subdivided into three parts: Title I on sales on credit terms, Title II on donations, and Title III on the "Food for Development Programme". Of these three, the most important was clearly Title I concerning disposal of stocks, in particular those held by the Commodity Credit Corporation, on very advantageous terms (very long-term credits - fifteen to forty years - very low interest rates of the order of 4 per cent to 5 per cent, small initial payment receipt of the goods - about 5 per cent).

2.15 He further said that if one examined the objectives of PL 480 as defined in the preamble to the law and its subsequent amendments, one found that while aid was one of the considerations invoked, it was far from being the only element justifying PL 480 sales. Indeed, the text stated that the various objectives pursued were, *inter alia*, to open new outlets for United States agricultural exports, to support United States agriculture and, in the long term, to promote the image of United States foreign policy. If one also looked at the beneficiaries of PL 480 sales one found that they were not really all developing countries (Portugal and in the past, Israel, Brazil, Japan, Spain) or were in a relatively favourable situation (such as South Korea). Furthermore, these sales were a very effective instrument of market penetration since it was customary for a country benefiting under PL 480 to undertake to reserve, in its future purchases, a "fair share" of its imports for products of United States origin, on current commercial terms (due counterpart); many countries, including Japan, Spain, Portugal, Brazil, South Korea had become paying customers for American agricultural products after having benefited under PL 480; and lastly, at least 50 per cent of the products exported had to be transported under the United States flag, which implied that the United States covered any difference in freight charges. It was clear, in these conditions, that sales under PL 480 did not constitute food aid exclusively and automatically but also comprised important commercial elements. In recent years PL 480 transactions had developed considerably, even to the detriment of what the United States itself called its commercial exports. In the case of flour in particular, United States exports under PL 480 accounted for about 70 per cent of the country's total deliveries. In these conditions he considered that it was not possible to exclude United States sales under PL 480 in the calculation of its exports and that it was impossible to disregard such sales when analysing changes in the world market and in particular the share held by the United States.

2.16 In including concessional sales in the "world trade" figure, the Community's intention was not to bring them under the disciplines of Article XVI of the GATT and Article 10 of the Code - although that question could well be examined in GATT. It was a question of interpretation of the terms and content of the obligations to be observed by any contracting party. It was also a question of equity; indeed, by disregarding non-commercial sales, the United States subtracted 10.8 per cent from total Community exports, whereas from its own exports it could subtract 70 per cent. Furthermore if all exports to developing countries were to be excluded from the concept of "world trade", the world market for flour would be virtually non-existent and virtually all EEC exports would be outside the GATT rules.

2.17 As regards determination of the previous representative period he considered that the United States' interpretation (see paragraph 2.8 above) was not acceptable because it was contrary both to the intention of the drafters of the Code and to the logic of the regulatory system that the Code was designed to establish. The drafters of the Code had never intended to exclude as "a previous

representative period" the years in which subsidies were granted, on the ground that the market would allegedly be functioning abnormally because of the existence of subsidies. The best proof that could be cited in this connection was the fact that, during the Tokyo Round, one delegation (Australia) had deliberately proposed that the grant of subsidies made market functioning abnormal, so that in determining normal market shares account should not be taken of a period in which subsidies had been granted (MTN/NTM/W/217/Rev.1). A number of delegations, including the United States, had opposed that proposal, which had consequently not been included in the final text. During the Tokyo Round negotiations the United States position had been that the representative period to be taken into consideration should be the most recent three or five years, leaving aside abnormal phenomena such as poor harvests because of drought, etc.

2.18 He also considered that the United States' interpretation did not correspond to the logic of Article 10. Indeed, one of the main characteristics of Article 10 was precisely that it did not consider export subsidies as unlawful but on the contrary accepted them when they met certain conditions. Accordingly, for the Code, the mere grant of export subsidies could not, in principle and automatically, render the functioning of the world market abnormal during the period in which those subsidies existed. Furthermore, the United States' interpretation led to impracticable consequences since, as was here the case, it meant referring to years several decades ago, in other words to a period for which it was very difficult to determine exactly whether or not subsidies of any kind had existed. If one followed the United States interpretation to its logical conclusion, one would have to refer to an initial period in which there was no export subsidization by any of the contracting parties, and not merely to a period in which the incriminated subsidy did not exist.

2.19 As regards determination of the effect of the alleged export subsidy on changes in shares of the world market the representative of the EEC considered that it had to be demonstrated for it was indispensable to proof of an accusation of having "more than an equitable share". Article 10:2(a) clearly specified that the expression "more than an equitable share of world export trade shall include any case in which the effect of an export subsidy granted by a Signatory is to displace the exports of another Signatory bearing in mind the developments on world markets". Consequently the Code intended that it should be demonstrated that it was the effect of the subsidy which had displaced trade flows and that, for the purpose, consideration must be given to other factors which might also be responsible for the developments on world market. The examination of other factors of change was, therefore, of capital importance, especially over so long a period as that envisaged by the United States. Such factors of change, which might explain developments in United States flour exports, were, first, the expansion of United States flour exports under PL 480 at the expense of its so-called commercial exports; secondly, the loss, sometimes a long time ago, of certain United States export markets for political reasons (for example: Sri Lanka, Egypt during a certain period, South Viet Nam, Syria, Libya); thirdly, the introduction in certain developing countries of local crushing capacity (cases of Jamaica and Sri Lanka), resulting in the replacement of purchases of flour by those of wheat - such introduction being most often financed by United States capital and associated with clauses for the purchase of United States wheat; and lastly, the particular structure of United States wheat flour exports, which was characterized by concentration (about 70 per cent) on three markets (Saudi Arabia, Sri Lanka, Egypt), where there were either PL 480 sales or the construction of flour mills, the remaining exports being marked by very great irregularity and influenced by PL 480 operations (which was reflected in a rapid expansion on certain particular markets such as Zaire, Sudan, or Somalia and a sporadic presence on other markets such as Nigeria and Indonesia).

2.20 He also said that account had to be taken of the factors of change in the Community's exports. First, EEC exports included also inward processing traffic (IPT), which did not involve refunds; such IPT exports had, however, experienced a considerable expansion in the last three or four years and accounted for an important share of total exports. Second, one could not disregard the existence and development of markets which were traditionally supplied from the Community because of historical

links with its Member States or of special economic and financial links (currency zones, co-operation agreements). Such markets, situated mostly in the countries of Africa, the Caribbean or the Pacific, were marked by the relative smallness and irregularity of deliveries and this enabled European suppliers - who sometimes had better shipping facilities (use of regular shipping routes, liners instead of special charters) and better market care - to enjoy trade advantages which had nothing to do with any effect of refunds. Consequently, if one added up the EEC flour exports to countries which for political reasons refused or were reluctant to be supplied from the United States and its exports to countries which constituted its traditional markets, one would find that the bulk of the growth of the Community's sales was concentrated in these two areas. That growth could not therefore be reasonably attributed to any effect of the refund. If it were enough to assume that the mere existence of an export subsidy entailed the displacement of exports, the consequence would be that any export subsidy for agricultural products, whatever its effects, would be prohibited. The Code did not, however, condemn all such subsidies but only those which had pernicious effects.

2.21 The representative of the European Communities further said that in relation to changes in shares of the world market US allegations ignored the following facts:

- that the "decline" in the market was actually due to the omission of food aid and the introduction of local flour mills in a number of developing countries, resulting in the transfer of purchases from flour to wheat, and very often United States wheat;
- that the "exclusion" of traditional United States exports was due, in addition to the two causes already mentioned, to the chronic saturation of United States milling facilities, which for years had been functioning at more than 100 per cent capacity<sup>1</sup> - so much so that United States operators were sometimes unable to deliver the quantities tendered for in third countries, even in cases exclusively reserved to them and these countries had to make use of the IPT system in the EEC for part of their contracts;
- that the inability of United States exporters to gain access to new markets was due, apart from the reasons already cited, to the absence of a trade network adapted to the needs and customs of those markets.

B. EEC export subsidies on wheat flour are applied in a manner which results in prices materially below those of other suppliers to the same market in violation of Article 10:3 of the Code

#### United States arguments

2.22 The United States representative contended that the EEC's complete dominance of world flour markets, achieved through the use of a subsidy which had been as high as 75 per cent of the US representative f.o.b. price, established a strong presumption of material price undercutting. The EEC could not have obtained such a dominant position were it not for its policy of granting whatever amount of subsidy was required to underprice its competitors and thus gain a particular market.

2.23 The representative of the United States said that data on specific 1980 and 1981 tenders 1981 tenders showed that the EEC had undercut the offer prices of the US and other suppliers in particular markets. He explained that data provided on certain specific tenders showed that the EEC had used export subsidies to undercut the prices of the US and other suppliers by very substantial amounts in several key markets in 1980 and 1981. He also said that flour quality and specification were detailed in the three tenders cited, and that all offers were thus for the same quality flour. He indicated,

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<sup>1</sup>The US representative pointed out that "more than 100 per cent capacity" has probably been calculated on the five-day week basis. In fact, the US industry has operated at about 80-88 per cent

capacity over the past ten years, based on the six-day week normally employed by the US milling industry.

however, that data on such tenders was difficult to obtain. There were relatively few public tenders in the world wheat flour trade, business usually being conducted through private arrangements. In addition, given the lack of success of US flour exporters in competing with subsidized EEC exports, US exporters had refrained from bidding in many cases.

2.24 The representative of the United States said that, in addition, data submitted by his delegation, demonstrated that the EEC export unit values for wheat flour were consistently below those of the US. He said that further data providing export unit values for specific markets over the 1976-1981 period, showed that EEC prices had consistently been below those of the US. These data were to support the US argument that the EEC had used export subsidies to displace US wheat flour exports and to gain an inequitable share of the world market. They also suggested that the price-undercutting demonstrated for specific tenders were not isolated instances but part of a systematic pattern. The US representative also drew attention to the high level of EEC export subsidies and to the fact that these subsidies were habitually higher than could be accounted for by the difference between world and EEC prices for wheat.

2.25 He said that there were no continuous export price data for wheat flour readily available for the period from 1962 to the present when EEC subsidies had been in effect. However, it was useful to examine export unit values to demonstrate comparative flour prices over the years, and to see how recent EEC underpricing was merely a continuation of a consistent practice in prior years. These unit values did not show the relative competitive positions with regard to individual transactions, but they did convincingly indicate the lower EEC price levels caused by export subsidies. In the circumstances unit values should be viewed as evidence of price undercutting. According to the statistical data in fifty-seven out of sixty months of the 1976-80 period at least one, and often several, EEC Member States had priced its wheat flour export to all destinations at levels below those of the United States. He considered that these statistics furnished proof that the EEC, with the help of export subsidies, had undercut US prices and thus had caused displacement of US exports in third country markets. These low export prices had enabled the EEC to gain more than an equitable share of the world market. He also considered that the lower EEC export prices could not be explained by any locational advantage on the part of the EEC. In cases where the EEC was nearer to the countries of destination and where its transport costs were therefore lower than those of the US, the EEC's locational advantage would not exist in the absence of export subsidies and its prices would still normally be higher than those of the US. Moreover, in many cases, where the EEC's transportation costs were higher than those of the US (e.g. to Jamaica), the EEC had still managed to underprice the US exporters.

2.26 He further said that the lower EEC prices had not resulted from the lower quality of EEC flour as compared to the quality of American flour. US exporters eager to obtain foreign markets would not have offered higher quality types of flour than those demanded, and tenders usually specified the quality upon which exporters based their bids. When US exporters bid against other suppliers, they were bidding on the same specifications for the same flour quality as the other suppliers.

#### EEC counter-arguments

2.27 The representative of the EEC observed that in three specific examples of price-undercutting cited by the United States no details were given concerning the qualities demanded, offered or accepted. It was well known that, in general, North American flours had certain qualities (amount of ash, moisture, protein content, bread-making characteristics) which required longer working time - machine time and standby, demanded special technical equipment, and definitely cost more on account of their protein content. However, some of the purchasing countries concerned were traditionally buyers of a different type of flour, better adapted to local bread-making methods and their food habits, which the European

suppliers were able to offer. Moreover, it was internationally recognized that demand for high-protein flour, of the kind supplied especially by the United States, had declined in recent years. European millers were, in general, able to adapt to local specifications and therefore offer flour which was of a different quality and less expensive. Objective and realistic comparison must therefore make allowance for price differences based on quality differences. Furthermore the prices quoted were C&F prices, i.e. they included freight charges. These charges were lower (about \$20 per ton) for shipments from Europe, if only because of the shorter distance. Here again, objective comparison had to make allowance for freight charges, i.e. be based on an f.o.b. price. Thirdly, reference was made in the United States complaint to the public price quotations in the trade, which were unanimously recognized and practised by the trade in and outside the United States. However a comparison of "US Gulf" prices f.o.b. of flour there quoted showed no significant difference with Community prices, while at the same time revealing a considerable difference with the prices, even f.o.b., of the United States "bids" on the markets in question. This led to questions about the exact circumstances surrounding these isolated, and certainly insufficient, "examples" of United States bids in markets in which US suppliers were not really present, except when operating under PL 480.

2.28 He also drew the Panel's attention to some factors which influenced price formation in the case of flour. In many developing countries there was a trend towards the introduction of local milling in order to create more jobs and to save foreign exchange. Whenever the price of flour was seen to be too high as compared to that of wheat there was danger of establishment of local milling capacity and of irremediable loss of the market. Consequently the price of flour could not go beyond a level representing a certain coefficient of the price of wheat. Another factor was sales under PL 480. These sales on easy credit terms defying all competition influenced, *inter alia*, the prices of flour on the normal market. In this relation he stressed that the selling of massive quantities of wheat under PL 480 constituted a powerful incentive for installation of local milling capacity. As a result PL 480 was creating a permanent source of uncertainty in world flour markets. A third factor related to the importance of supplementary costs of transporting and loading and unloading flour. Here it was important to note that such costs depended not only on distance but also on the volume and regularity of deliveries. Thus, American flour mills, which worked primarily for the domestic market and which were sited to serve that market, found themselves penalized by the costs of storage (which were very high in the United States), of forwarding and especially of domestic transport within the United States, in addition to international transport. For numerous markets the United States could not use regular shipping lines and must resort to charters - which completely excluded deliveries in small quantities.

2.29 As to the argument that the complete dominance of world flour markets achieved by the Community through the use of export subsidies established a strong presumption of price undercutting, he said that the relevance of such an argument to prove a violation of Article 10:3 was questionable, for that provision related only to particular markets, which must be specified, and applied only to sales at prices materially below those of principal competitors for the same market. But that was not how the accusation was formulated and the plural "world flour markets" was deceptive; what the United States probably meant was domination of the world market - a point that might perhaps be relevant to paragraph 1 of Article 10 but in no case to paragraph 3 of that Article. Furthermore, he considered that the effect of the "subsidy" had not been demonstrated at all and that "domination", if there was domination, was in itself no proof that the dominator was "undercutting" prices; the Code was not concerned with such a possibility. And, besides, since the United States largely dominated the world wheat market (whether or not flour was included), did it necessarily follow that it was because the United States "undercut" prices?

2.30 As regards the use of data based on export unit values for wheat flour to support an accusation of price undercutting by comparing United States export unit values with those of various Community Member States, the representative of the EEC disputed the reliability of such a method in an exercise of this kind. He stressed the absence of any precise indication of methods of calculation, estimation or

kind of prices used. In addition, no details were given concerning qualities, quantities, or conversion rates. When one considered the wide variations that could occur in the price of wheat flour depending on the time of year or the country concerned, if only because of the current price of wheat and of demand situation whether general or particular in the market of destination, such imprecision could only invalidate the results. If one added to this aspect the absence of data on quantities actually traded, such an exercise became purely artificial and totally divorced from market realities.

2.31 As regards the reference to the level of EEC export refunds with respect to prices of wheat, he said that the facts refuted the US accusation according to which the EEC refunds were considerably in excess of the calculation basis corresponding to the difference between world prices and internal prices for wheat.

C. EEC export subsidies on the export of wheat flour result in nullification or impairment of the benefits accruing to the United States under the GATT and are causing serious prejudice to the interests of the United States in terms of Article 8 of the Code

#### United States arguments

2.32 The United States representative said that nullification or impairment of benefits accruing under the GATT resulted from EEC violation of the requirement in the GATT and the Code that EEC export policies should be conducted in a manner consistent with its obligations under GATT Article XVI and Articles 8 and 10 of the Code. Referring to Footnote 26 to Article 8:4 of the Code he said that the EEC had clearly violated these obligations, that it had consequently nullified or impaired benefits to the US and other major exporters, and that adverse effects might be presumed to exist. Furthermore Article 8:3(c) of the Subsidies Code provided that Signatories should seek to avoid causing, through the use of any subsidy, serious prejudice to the interests of another Signatory. It was noted that serious prejudice had the same meaning as in Article XVI:1 of the GATT and included threat of serious prejudice. Article 8:4(c) stated that the adverse effect needed to demonstrate serious prejudice might arise through the effects of the subsidized exports in displacing the exports of like products of another Signatory from a third country market. Taking all this into account he contended that the EEC subsidy system for wheat flour had seriously prejudiced, and threatened to continue to cause serious prejudice, to the trade interests of the United States and other wheat flour exporters. He noted that the US contention that the EEC subsidy system had had the effect of displacing US exports in third country markets had already been demonstrated.

2.33 He also said that the effect of the EEC system in creating a permanent source of uncertainty in world flour markets demonstrated that the EEC's subsidization had seriously prejudiced the interests of other exporters within the meaning of Article 8:3 of the Code. He recalled that in reviewing a recent complaint by Australia against the EEC for its export subsidies on sugar, the panel had concluded that the EEC's system constituted a permanent source of uncertainty in world sugar markets because of the absence of pre-established limitations of EEC production, prices, and export refunds; and, hence, constituted a threat of serious prejudice in terms of Article XVI:1 (BISD, 265 page 319 paragraph h). He considered that this finding provided a precedent upon which to base a decision that the EEC's export subsidization of wheat flour had seriously prejudiced and continued to threaten serious prejudice to the interests of other wheat flour exporters within the meaning of Article 8:3. As in the case of sugar, the EEC Commission had no pre-established limitations on wheat flour production, prices, and export subsidies. Hence, on the basis of the panel decision on sugar alone, it was clear that the EEC subsidies on wheat flour constituted a threat of serious prejudice.

2.34 He further said that the uncertainty created by the fact that the EEC had no pre-established limits on its subsidy mechanism was compounded by the arbitrary manner in which the EEC established its export subsidy levels. The EEC flour price used in establishing the amount of the export subsidy was

arbitrarily selected from nine or ten prices. Furthermore, such prices were in fact derived from wheat prices and not based on actual market prices of wheat flour. In deriving those prices, the EEC at several points in the calculation indicated amounts attributable to expenses such as transportation, bagging, weighing, etc., which might bear no relation to the actual cost of these expenses. Because of the method by which the subsidy was calculated, the EEC created substantial uncertainty in world flour markets through the administration of the subsidy. Neither the importer nor other competing exporters could anticipate the level of the EEC subsidy. The costs of production which dictated competitiveness in the market place were only dimly reflected in the EEC price of flour calculated by the Commission and in EEC offer prices. Hence, other exporters could not anticipate the level of the EEC bids and were unable to compete. He also considered that the EEC's arbitrary approach in setting the level of the subsidies resulted in excessive subsidization which further prejudiced the interests of other wheat flour exporters.

### EEC counter-arguments

2.35 The representative of the EEC pointed out that the word "seek" at the beginning of Article 8:3 had a very precise legal meaning. It signified an obligation as to means and not results. Nevertheless, he considered, in the present case, that that aspect might seem secondary inasmuch as the substance of the accusation was unfounded. The "serious prejudice" allegedly caused to the interests of the United States was held to be due to "the effects of the (EEC's) subsidized exports in displacing exports of like products (of the United States) from a third country market". In this connection the United States relied on sub-paragraph (c) of Article 8:4. In doing so, it simply disregarded Note 28, which specified that, so far as primary products were concerned - to which flour undoubtedly belonged since it was crushed wheat - the problem of third-country markets was dealt with exclusively under Article 10. Therefore, the argument based on sub-paragraph (c) of Article 8:4 must be legally regarded as inapplicable to the case.

2.36 He said that as regards the substance this legal exclusion did not change much, for the assertions made in support of the alleged "prejudice" were the same as those advanced in support of the accusation of violation of Article 10 which, in his view, he had already amply refuted.

2.37 He further observed that the United States charge that it suffered a prejudice from the "arbitrary manner in which EEC export subsidies for flour were set" had no basis in the Code. The Code did not, in any case, prescribe "any pre-established limits on production" in connection with export subsidies. The EEC could not, by any means, accept such a modification, of its obligations. As to the "lack of any pre-established limits on EEC prices or subsidies", the argumentation had no basis since on that point the EEC's obligations resulted from paragraphs 1 and 3 of Article 10, and he considered that the EEC had previously shown that it had complied with those obligations. Moreover, here again, he noted the total absence of any material evidence.

2.38 With respect to the nullification or impairment of benefits accruing under the General Agreement he observed that, under the very terms of Note 26, it was after the Committee had determined that there had been a failure to carry out obligations under the Code or the General Agreement that adverse effects might be presumed to exist. He considered that the United States accusation was therefore premature in this respect, and, somewhat out of place in view of the weakness of its argumentation.

### III. Factual Aspects

#### (a) EEC export refunds on wheat flour

3.1 Provisions relating to the modalities of application and criteria for fixing the amounts of export refund on wheat flour are part of the basic EEC regulations on the common organization of the market in cereals which provides, inter alia, for the free movement of the produce within the Community.

3.2 After a transitional period from July 1962 to June 1967 (Regulation No. 19/62 EEC of 4 April 1962), the common organization of the market in cereals and cereal-based products was originally established by Council Regulation No. 120/67 EEC of 13 June 1967. The single market in cereals came into force on 1 July 1967.

3.3 Council Regulation No. 120/67 (as amended) remained applicable until the marketing year 1974/75, when it was replaced by Council Regulation (EEC) No. 2727/75 of 29 October 1975 which came into effect on 1 November 1975. This regulation (as amended) is still in force.

3.4 The common organization of the market in cereals provides a single system of internal prices valid for the whole Community, and a common trading system with third countries which is designed to prevent price fluctuation on the world market from affecting cereal prices ruling within the Community.

3.5 In the case of wheat flour, the Community internal price régime consists of a series of price mechanisms designed to maintain an indicative or "target" price for common wheat within the EEC, as well as to ensure the protection of the Community milling industry. As part of the system established to achieve these ends, a threshold price for wheat flour is calculated each year, with periodic adjustments as necessary. The price level thus established serves as the internal EEC price standard for purposes of the Community trading régime.

3.6 The Community trade régime for wheat flour provides for import and export licensing, and for application of import levies and export refunds under certain conditions and in a prescribed manner. Import or export licences are issued by Member States and are conditional on the lodging of a deposit guaranteeing that importation or exportation will be made during the period of validity of the licence. This period covers the month of issue plus four months (end of the fourth month).

3.7 In the case of import of wheat flour into the Community from third countries, a levy is charged which is equal to the threshold price less the import c.i.f. price, normally calculated for Rotterdam on the basis of the most favourable purchasing opportunity on the world market, with appropriate account being taken of differences in quality.

3.8 General rules for granting export refunds on cereals (including wheat flour) are contained in Regulation (EEC) No. 2727/75. Under this regulation, an export refund may be granted where necessary to cover the difference between the established price for wheat flour within the Community and those prevailing on third markets.

3.9 Regulation No. 2746/75 lists three specific criteria for fixing export refunds on wheat flour, notably:

- i. common wheat prices ruling on the various Community markets;
- ii. the quantities of wheat required for the manufacture of wheat flour and the value of by-product;
- iii. possibilities and conditions for the sale of wheat flour on the world market.

3.10 In practice, the mechanism described in the regulation for fixing the refund works as follows:

- a) The first two criteria are aimed at determining the cost price f.o.b. European port for wheat flour in bags. An announcement is made weekly for each Member State of the market price for domestic milling wheat delivered to mills. This wheat price is then converted by the Commission into a flour price by means of fixed coefficients relating to the quantity of wheat

needed to make 1 ton of best quality EEC type flour, the millers' profit margins, the value of the milling offals, and costs incurred for bagging the flour and putting it in on a f.o.b. position. This calculation results, for the whole Community, in a range of f.o.b. wheat flour prices, which are different according to the export points. From this range of calculated prices the Commission selects a price as representative of Community prices (f.o.b.) for wheat flour for purposes of calculating the level of export refund for the Community as a whole. As a general rule, the French prices are selected because France is the EEC Member State with the largest surplus of common wheat; it exports most common wheat and flour to third countries, and Rouen is the leading European port for the export of cereal and flour.

- b) The third criteria is aimed at determining other countries' export prices for wheat flour, according to the available information. This determination is made essentially on the basis of world prices for wheat (notably common wheat of a quality comparable to that of European wheat), as the cost of wheat is regarded by the Community producers as the major factor for establishing the price of flour. Certain additional elements are also taken into account, including wheat flour export prices of other suppliers to the extent these are available.

3.11 The Commission fixes the level of export refund based on its assessment of the foregoing information and calculations in light of the relevant EEC Regulations. A regular price study is made weekly, but the rate of refund generally remains unchanged for longer periods modifications are made in the refund level when the difference between EEC wheat flour prices and other wheat flour prices changes to a significant degree.

3.12 The level of export refund on a particular shipment of wheat flour is normally that applicable on the day of exportation. However, when applying for an export licence, an exporter may request that the export refund be fixed at the level applicable on the date of the licence application. Such a refund level could be applied to a shipment at any time during the 4-5 month period of validity of the licence, adjusted on the basis of changes in the threshold price which reflects changes in the price of wheat. This procedure is called advance fixing.

3.13 The export refund on wheat flour may also vary according to destination where this is required by the world market situation or by the specific situation of certain markets. This provision was used mainly in the first years following the introduction of export refunds on wheat flour. In the most recent period, however, it has been used only once, in 1981, to lower and eventually eliminate the export refund to the USSR.

3.14 The funding of the export refund on wheat flour is made by a public contribution out of the budget of the Communities (EAGGF) from the same budget allocation used for the export refund on wheat in the natural state.

(b) Basic features of the world wheat flour market

3.15 Wheat flour is a commodity which is neither uniform nor homogeneous as it basically derives its quality characteristics from the grades of wheat (hard, medium-hard, soft, etc.) or blends thereof used for its production, and the milling processes by which successive stages of refinement may differentiate its types.

3.16 A wide variety of types of wheat flour can, therefore, be produced and traded internationally to suit differing requirements of importing countries, or particular users within each country. Among those types a distinction can be drawn between hard flours which are produced from more expensive, high-protein hard wheat grades, and soft flour which are produced from mainly cheaper, low-protein soft wheat grades. Actually, types of wheat flour traded differ considerably among major exporting countries.<sup>1</sup>

3.17 In the post-war period, world trade in wheat flour rose from an average of about 4.5 million metric tons in the early 1950's to an average of about 5.5 million metric tons in the 1970's.<sup>2</sup> At the same time, however, its relative importance vis-a-vis wheat trade decreased sharply, notably during the 1970's when world wheat trade expanded considerably and a shift from flour to wheat took place in many importing countries, following the establishment and further development of a domestic milling industry.

3.18 During the same post-war period, the patterns of wheat flour trade also changed in important respects. As regards imports, whereas, developed countries had been the largest markets for wheat flour in the early 1950's, they accounted for only a small share of total imports by the 1970's. At the same time imports by developing countries have grown, accounting by the 1970's for more than nine-tenths of wheat flour imports. The most rapid increases have taken place in Africa and Asia, particularly in the Middle East.<sup>3</sup>

3.19 Relative shares in total export trade have changed as well since the 1950's with the trend being an increase in the relative export market share of the EEC, and a decrease in those of other exporters (cf. Table V). The bulk of world wheat flour exports continues, however, to originate in a limited number of countries, notably Australia, Canada, the EEC, and the United States. As exporters, they have all faced a number of factors which have increasingly characterized the world market in recent years; notably

- (i) A small number of large markets with greatly varying imports of wheat flour from one year to another;
- (ii) A large number of small markets;
- (iii) A number of importing countries which enter the international market only on an irregular and unpredictable basis;
- (iv) The propensity among developing countries to establish and increase their own milling capacity, as noted in paragraph 3.17.

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<sup>1</sup>Australian flour is basically a mixture from both hard and soft wheat, but some high-protein hard flours are also exported. Canada exports mainly high-protein hard flour from CWRS wheat grades. EEC's wheat exports is almost exclusively made of low-protein soft flours. No breakdown of exports by types of flour is available in the case of the United States.

<sup>2</sup>cf. Table III

<sup>3</sup>In recent years, Egypt, Saudi Arabia, Sri Lanka, Cuba, Syria, Vietnam, India, Algeria and Libya were the major flour importing countries. Together, they accounted for about two-thirds of total wheat flour imports. The remaining was taken almost exclusively by more than 70 other developing countries

and the USSR.

TABLE V  
Percentage Share of World Wheat Flour Exports by Major  
Wheat Flour Exporting Countries

(July/June Years)

	1950/51	1960/61	1970/71	1980/81
Australia	22	14	8	2
Canada	34	17	14	8
EEC	8	16	37	66
United States	34	52	31	21
(of which: commercial	(34 )	(15 )	(5 )	(6 )
special	(-)	(37 )	(26 )	(15 )
Others	2	1	11	2

Source: cf. Table III and IWC, secretariat paper No. 5

3.20 Since the mid-50's, a certain amount of wheat flour from all major exporting countries has entered international trade under conditions not conforming to usual commercial practices. These shipments were made originally in connection with surplus disposal of accumulating stocks. From the early 1960's such shipments have been made in the context of government programmes aimed at providing commodities either as gifts or on concessional terms of sale to developing countries. With few exceptions, countries currently receiving wheat flour on special terms are also importers of wheat and flour on commercial terms. In recent years, such special transactions have represented about one-fifth of world wheat flour export trade. In the case of the United States, under PL 480 programmes, they have accounted for more than two thirds of the country's total wheat flour export; between one fourth and one third in the case of both Australia and Canada; and for about one tenth in the case of the EEC<sup>1</sup>.

3.21 As early as in the 1950's, the export of commodities (including wheat flour) on other than normal commercial terms was recognized as creating uncertainty in commercial markets. As a result, the FAO Principles of Surplus Disposal were adopted in an effort to minimize such effects. These principles serve as the basis for notification and consultation procedures in the FAD Consultative Sub-Committee on Surplus Disposal (CSD).

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<sup>1</sup>These figures include food aid as outright gifts. Due to the lack of a common definition of food aid, however, it is not possible to single it out accurately. In the case of the EEC, for example, special transactions consist only of food aid as outright gifts; while, in the case of the United States, in the last years, food aid as outright gifts has represented about one third of total special transactions, accounting for 20-25 per cent of total United States wheat flour exports, the remaining special transactions being

sales on concessional terms.

3.22 Wheat flour prices in domestic markets are determined by a number of factors, such as the cost of wheat, which is the major single pricing element for flour, and of other inputs, the market value of by-products, marketing and other commercial costs, and the supply/demand situation which can differ considerably from one country to another as well as in given country from one year to another. As a result, not only do different types of flour normally vary in prices according to quality characteristics<sup>1</sup>, but also a given type and quality of flour is often subject to sharp price fluctuations.

3.23 Government involvement in the grains sector, to a varying extent and by different methods, is also a common feature in all major exporting countries. The broad outlines of the EEC systems are set out in paras 3.2 to 3.15. In the other major exporting countries Australia, Canada and the United States, government involvement as it relates to wheat flour is reflected primarily or exclusively in the price at which millers obtain their wheat, because of national price and support policies for wheat.

3.24 As regards wheat flour prices in the international trade, a world price for flour does not exist, at least in the sense it does for other internationally traded commodities, such as wheat, coffee, sugar, cocoa, etc. nor is there a futures market for wheat flour. Published quotations do not represent specific, individual market transactions, but reflect rather an average of such transactions. Wheat flour export prices are fixed freely by the exporters on the basis of their own appreciation of the market, consideration being given *inter alia*, to factors relating to domestic prices for heat flour (cf. paragraph 3.22), the availability of export payments, the quantity of flour involved in the shipment, transportation and other handling costs, and also the price level of wheat in the importing country. Broad price differences can, therefore, occur in a given market for a given type and quality of wheat flour. These differences in prices are normally sharpened by differences in the quality of wheat flour. Little is known, however, on actual prices paid for individual deliveries. Most transactions are concluded by means of tenders to which little publicity is given. Usually, only the price of the winning tender is known, as private firms generally consider pricing to be a confidential matter.

#### IV. Findings

4.1 The Panel carried out its consideration of the matter referred to it by the Committee for examination in light of the terms of reference as expressed in paragraph I.1.A. It has based its consideration on:

- (a) the facts of the matter as presented by the parties to the dispute, and information which was available to it;
- (b) arguments presented to it by the parties to the dispute;
- (c) the relevant provisions of the Code.

4.2 With regard to the United States' assertion in its presentation to the Panel that EEC export subsidies on wheat flour are *prima facie* contrary to Article 9 of the Code, the Panel was of the opinion that this question did not constitute part of the matter referred to the Panel by the Committee and therefore the Panel did not consider the substantive issue involved.

4.3 When examining the Community system for granting refunds on exports of wheat flour, the Panel noted that such refunds were financed out of the EAGGF - Guarantee Section and that, in the sense of Article XVI:1, they operated to increase exports of wheat flour from the Community. The Panel therefore concluded that the granting of refunds by the EEC on exports of wheat flour must be considered a form of subsidy and subject to the provisions of Article XVI of the General Agreement as interpreted and applied by the Code.

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<sup>1</sup>Notably the extraction rate, the protein content, the percentage of ash, acidity and colour.

4.4 The Panel therefore addressed itself in particular to whether the application of the subsidy has resulted in:

- (A) the EEC having more than an equitable share in world export trade in wheat flour, in terms of Article 10:1 and 2 of the Code;
- (B) prices materially below those of other suppliers to the same market in terms of Article 10:3;
- (C) nullification or impairment of benefits accruing to the United States, or serious prejudice to the interests of the United States under the Code.

(A) Article 10:1 and 2 of the Code: (equitable share)

4.5 The Panel noted that in GATT there was no precise definition of "more than equitable share of world export trade" or detailed guidelines as to how that was to be determined.

4.6 The Panel proceeded in its examination along the following lines:

1. Shares of world export trade;
2. Developments on the wheat flour market:
  - (a) General observations
  - (b) Special factors
  - (c) EEC Refund Mechanism
3. Market displacement

1. Shares of world export trade in wheat flour

4.7 In examining shares of world export trade, the Panel considered global exports from all sources, to all markets, on the basis of statistics compiled by the International Wheat Council in its Record of Operations. The Panel noted that trade in wheat flour takes place under commercial and special (or concessional) terms. For purposes of its examination of market shares the Panel considered that it was difficult to exclude special transactions entirely from an analysis of the market, and that in this case, it was not necessary, or appropriate, to do so in reaching a determination as to equitable share.<sup>1</sup>

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<sup>1</sup>See paragraph 3.20, footnote 1, and paragraph 3.21 for a factual note on outright gifts. There is also a useful discussion of the difficulties inherent in distinguishing between commercial and non-commercial transactions, in the FAO's Principles of Surplus Disposal and Consultative Obligations of Member Nations. The Panel, while being cognizant of these difficulties and the issues involved therein, did not regard it as necessary to draw conclusions of general application on them in this case. If one excludes special transactions, the magnitude of changes in the market is amplified, but the basic pattern of market changes is similar whether they are included or not, i.e., the Panel did not consider that in this case inclusion or otherwise would be a critical determinant as regards changing market shares. On the other hand, given the volume of special transactions and its importance in overall market

developments, the Panel was of the view that these shipments could not be ignored.

4.8 In light of the provisions of Article 10:2(c) of the Code, the Panel first compared world market shares in the three most recent crop years<sup>1</sup> prior to the US complaint under the Code, i.e., 1977/78, 1978/79 and 1979/80 with market shares in 1980/81.

TABLE VI

(1,000 Metric Ton Wheat Equivalent)

	<u>1977/78</u>	<u>1978/79</u>	<u>1979/80</u>	<u>1980/81</u>
Australia	160	114	97	135
Canada	783	818	693	547
United States	1,539	1,462	1,487	1,394
EEC*	3,096	3,280	4,125	4,404
Other	157	115	297	153
Total:	5,735	5,789	6,699	6,634

Source: Table III.

\*EEC figures do not include EEC exports of wheat flour under the IPT system for which a breakdown by destination is not available. IPT exports, which are not reported to the IWC, are generally estimated on the basis of official imports of wheat under the IPT system.

4.9 The market share of the EEC over this period was:

1977/78	- 54 per cent
1978/79	- 57 per cent
1979/80	- 62 per cent
Average 1977/80	- 58 per cent
1980/81	- 66 per cent

4.10 The EEC increase in market share in 1980/81 over the average three-year period was 14 per cent. In absolute terms, the net increase in EEC shipments in 1980/81 over the grievous three-year average was 903,667 metric tons, a 26 per cent increase.<sup>2</sup>

<sup>1</sup>Although the Code calls for calendar years both the data provided by the complainant and the IWC data used by the Panel were based on crop years. The Panel was of the opinion that the use of crop instead of calendar years would in no way affect its findings.

<sup>2</sup>See Annex (A) for an indication of significant EEC increases and decreases in individual markets

in 1980/81, as compared to the previous three year average.

4.11 The Panel was of the view that while the three most recent year period was in many ways instructive as regards important aspects of trade in wheat flour, it did not in itself provide a fully satisfactory basis for determining "equitable share". Market shares in this period, as indeed for virtually any period in at least the last twenty years, had been affected by the application of export subsidies<sup>1</sup> and other developments in the market, the full import of which could be properly taken into account only by examining other periods as well.

4.12 After examining a number of other possibilities of representative periods the Panel found that while there were some differences between the three most recent years and earlier periods, the fundamental picture of market developments tended to be consistent.

4.13 If for example one compares the relative positions in the world market during the three years prior to the Community-wide application of export subsidies, with the last three years, the overall increase in the EEC shipments and share of the market (which itself had only increased by 3 per cent) was significant (see table below).

TABLE VII  
(1,000 Metric Tons Wheat Equivalent)

	63/64-65/66	78/79-80/81	% change in volume
Australia	691	116	- 83%
Canada	1,137	686	- 40%
United States	2,462	1,448	- 41%
EEC	1,465	3,936	+ 169%
Other	430	188	- 56%
Total	6,185	6,374	+ 3%

Source: Table III.

<sup>1</sup>See Report of the Working Party on Other Barriers to Trade, adopted by CONTRACTING PARTIES on 3 March 1955. (BISD. 3S p.226). Member States of the EEC had applied export subsidies for a certain period before 1967. Since that time the EEC export refund system has been operated by the Commission on a Community-wide basis. The United States provided export subsidies

on wheat flour for a certain period until 1974.

	<u>Market Share</u>		<u>Percentage change</u>
Australia	11%	2%	- 82%
Canada	18%	11%	- 39%
United States	40%	18%	- 55%
EEC	24%	62%	+ 158%
Other	7%	3%	- 57%
Total	76%	38%	- 50%

4.14 Relative changes in market shares over this period can be seen in the following graph:

PERCENTAGE OF WORLD FLOUR MARKET

[Graph]

4.15 It is evident therefore that the EEC share of world exports of heat flour has become larger over a time period when payment by the EEC of export subsidies was the general practice.<sup>1</sup>

2. Developments in the Wheat Flour Market

(a) General observations - basic features of the world flour market

4.16 Before examining particular phenomena which might be regarded as "special factors" in the sense of Article 10, the Panel considered a number of general features which in its view were of fundamental importance in understanding developments in the world wheat flour market, and the rôle of export subsidies therein.

- (i) There has been a significant trend, based on political and economic factors, toward increased domestic milling capacity throughout the world. This meant that in the past twenty years the wheat flour market has grown very slightly (to a total in 1980/81 of some 6,634,000 metric tons) while that of wheat has more than doubled (to a total in 1980/81 of some 80,505,000 metric tons).<sup>2</sup> Associated with this development, there has been increased sensitivity as between wheat and flour prices, i.e. in general, the propensity toward wheat imports has meant that wheat flour prices must be maintained within a certain margin to those of wheat - otherwise the shift from flour to wheat is likely to be hastened.

<sup>1</sup>The exceptions were from 30 May 1973 to 3 August 1973, 6 August 1973 until 1 February 1975, and 1 August 1975 to 3 December 1975, at times when the world market situation strengthened to a point where export price levels rose to those established within the EEC, obviating the need for export assistance. World prices strengthened to the point that from November 1973 to December 1974, export levies were applied to ensure that internal supplies at established prices were met.

<sup>2</sup>See IWC Record of Operations, 1980/81.

- (ii) It is noteworthy that relatively little of world trade in wheat flour takes place on the basis of the free play of the market. In recent years, the bulk of EEC and US shipments (which together account for more than four-fifths of total world exports of wheat flour) were made either under export subsidies or under non-commercial transactions. Thus both the levels and conditions of trade in wheat flour are highly artificial.<sup>1</sup> It is apparent that with these various measures the market for wheat flour has been maintained at a higher level than otherwise might have been expected.
- (iii) Developments in the world wheat flour market might in some respects be characterized as chaotic due to the existence of a few important markets with greatly varying imports from one year to another, a large number of small markets, some of which import only on an irregular and unpredictable basis<sup>2</sup>, the absence of recognized world prices, and the sometimes broad price differences in a given market for a given type and quality of wheat flour.<sup>3</sup>
- (iv) The opening of lines of credit at highly reduced interest rates and/or other forms of government supported deals concluded within a framework of bilateral or other arrangements have sometimes been the major factor influencing the conclusion of transactions. This practice may have been particularly relevant in the Egyptian market in recent years, the largest single market for flour.

(b) Special factors

4.17 Taking into account these basic features of the world flour market the Panel considered in a detailed examination of market developments the extent to which a number of special factors, including those presented by the EEC, may have had a bearing on market shares.

(i) Political developments

4.18 Political developments, such as embargoes or changes in diplomatic relations, have played an important rôle at times in hindering US flour sales to a number of countries and in affecting relative market shares as between the EEC and the US. This has been the case for certain extended periods in Angola, Cuba, Libya, Vietnam, North Korea and, as a direct result of the US grains embargo, in the USSR in 1979/80, and in particular, in 1980/81. After no shipments to the USSR in 1977/78 and 1978/79, EEC exported 123,348 metric tons in 1979/80, and 702,651 metric tons in 1980/81. Substantial EEC increases in volume terms in 1980/81 over the previous three-year average were registered in the following markets where the US exports were disadvantaged on political grounds:

USSR	-	661,000	metric tons	
Libya	-	117,000	"	"
Angola	-	76,300	"	"
		-----		
		854,300	"	"

4.19 Political developments may also have affected US shipments one way or the other in particular years in Egypt and Sri Lanka, but the Panel was not in a position to determine whether this resulted in longer term changes in the pattern of supply.

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<sup>1</sup>cf. also paragraph 3.23.

<sup>2</sup>cf. paragraph 3.19.

<sup>3</sup>cf. paragraph 3.25.

(ii) Non-commercial sales

4.20 The Panel noted that during the period under review the levels of wheat flour entering international trade under conditions not conforming to usual commercial practices, and the proportion of total wheat flour imports which were accounted for by such shipments, were considerable.<sup>1</sup> The Panel considered that such a development could have important consequences for the commercial market in the broad perspective, notwithstanding agreed mechanisms for limiting such consequences within individual markets.

4.21 The Panel considered that one of the possible effects<sup>2</sup> of large concessional sales was that of market creation, i.e. the development of an import requirement over time at levels higher than would otherwise have occurred under purely commercial conditions. The Panel found however that conclusions as to the impact on changing market shares of such an effect were less than clear. On the one hand, it could not be ruled out that, once accustomed to the quality supplied and business relations established under concessional sales, importers would have a tendency to continue to buy from the same source under commercial conditions, or under a mixture of concessional and commercial terms. On the other hand, there is some possibility that when concessional sales have been reduced or withdrawn, importers have been unable or unwilling to purchase comparable quality on commercial terms, and have turned instead to EEC flour at lower prices.

(iii) Regular shipping lines

4.22 The Panel noted that about one-fourth of the wheat flour market was accounted for by a large number of small markets including importing countries which enter the international market only on an irregular and unpredictable basis. Many of these markets are located in the Middle East and Africa. The Panel considered that the existence of regular shipping lines from EEC Member States to most of these countries could be an important factor in permitting the transportation of small quantities of flour and in meeting irregular and unpredictable purchases at reasonable costs. In particular, it could facilitate the observance of times of delivery, which may play an important rôle in maintaining longer term business relationships between importer and exporter. The Panel noted that those major suppliers not benefitting from regular shipping lines, may suffer some disadvantages vis-à-vis EEC exporters in these markets.

(iv) Other factors

4.23 The Panel was aware of a number of other factors which might be of a certain relevance to developments of market shares. The effects of such factors, inter alia, historical links, cultivation of "traditional" markets, particular taste or dietary demands, trade practices of respective traders and increased domestic milling capacity (in addition to its influence on price levels) are however difficult to establish with any assurance).

4.24 With respect to shipping costs the Panel noted, that the EEC is located in the proximity of the most important and expanding markets for wheat flour, namely the Mediterranean and Middle Eastern areas. Other markets in certain South American and Caribbean countries such as Barbados, Chile, Jamaica and Trinidad and Tobago are however close to the USA. The Panel was of the view that although transportation costs may have a certain effect with regard to shipments to specific destinations they should be considered of minor importance in the overall assessment of market share developments.

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<sup>1</sup>cf. paragraph 3.20.

<sup>2</sup>cf. FAO - Principles of Surplus Disposal and Consultative Obligations of Member Nations.

4.25 The Panel also examined whether the quality of EEC wheat flour constituted a certain advantage for the EEC, given developments in the market and the need for competitive pricing. Apart from some 10 per cent produced from imported, higher quality wheat, EEC flour entering international trade is produced from domestically grown soft wheat which on the world market commands a lower price than hard, higher protein product. Noting the generally higher, pre-established internal EEC price, the Panel found however that EEC wheat flour was not "lower price" without the benefit of the export subsidy under the refund mechanism. The Panel therefore considered that the quality of EEC wheat flour, per se, was not a factor which helped explain the EEC increase in market share.

(c) EEC Export Refund Mechanism

4.26 As noted in the description of the refund mechanism (paragraphs 3.2 to 3.13) there are a number of points in the process of fixing the refund levels where calculations of a technical nature are made - such as the coefficient used for translating wheat into flour prices, the value set for by-products, and the estimation of costs of placing wheat flour into FOB position. The Panel was not in a position to assess the validity and accuracy of such calculations, but noted that these elements were of importance in establishing the price level on the basis of which EEC wheat flour enters the report market and that on the basis of information available and arguments made to the Panel such calculations, at least in some instances could be open to technical debate. In addition, the Panel considered that the basis used for determining "Prices ruling outside", and judgemental aspects involved in the final setting of and subsequent corrective adjustments to the export refund may give rise to similar questions in this context.<sup>1</sup>

4.27 The Panel also considered that in a market situation in which there is downward pressure on prices<sup>2</sup>, the EEC export refund mechanism may provide the EEC trader with a certain advantage vis-à-vis other suppliers, in that it subsidizes the export to the extent necessary to meet lower price levels of wheat flour. This may further contribute to the downward pressure on prices.

3. Market displacement

4.28 The Panel found that, despite the considerable increase in EEC exports, market displacement in the sense of Article 10:2(a) was not evident in the seventeen markets presented by the USA and examined by the Panel.<sup>3</sup>

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<sup>1</sup>See Annex (B) for a discussion of difficulties involved in determining international price levels required for the establishment of export refund levels.

<sup>2</sup>The relationship between wheat and wheat flour prices in face of a trend toward domestic milling, as noted in paragraph 4.16, has had an effect in this regard, as had the situation of relative

oversupply for much of the period under review. Large volumes of non-commercial transactions have probably had a price depressing influence as well, notwithstanding international understandings intended to limit their effect on normal commercial sales.

<sup>3</sup>See Annex C.

4.29 The Panel noted that, when viewed over the time period suggested by the US (from 1959/60)<sup>1</sup> there were several markets<sup>2</sup> in which in the earlier three year period the US was in a stronger position than the EEC, whereas in the most recent three years the EEC was in the stronger position. These markets however had changed considerably in size and nature over such a long period, and the changes in market share were such that cases of displacement in the sense of Article 10:2(a) was not evident. There were a number of markets<sup>3</sup> where US commercial shipments had not been particularly significant in the earlier years, and in which the EEC has in recent years obtained all or most of the commercial growth. Finally, in Jamaica the EEC share has increased but not so much at the expense of the US as of other suppliers. Jamaica is a declining market where the EEC has been able to maintain and sometimes increase its volume of exports and thus obtain a relatively larger share of the market. The Panel considered that the foregoing developments were not to be seen so much in terms of Article 10:2(a) and (b), but rather as being indicative of the growth of the EEC share of the market more generally. The Panel found in its examination of individual markets that it could not rule out the possibility that the application of EEC export subsidies had resulted in reduced sales opportunities for the United States.

B. Article 10 (Price undercutting)

4.30 The Panel examined the US argument that EEC export subsidies on wheat flour are applied in a manner which results in prices materially below those of other suppliers to the same market in violation of Article 10:3 of the Code.

4.31 The Panel noted that three of the eight specific cases<sup>4</sup> presented by the US were qualified as being "reported" or "estimated". As the Panel was not in a position to ascertain the accuracy of these three cases it did not consider them further.

4.32 As regards the remaining five cases, the Panel considered that as the offers were made in response to specific tenders, there was a certain presumption that the transactions were comparable for purposes of Article 10:3.

4.33 The Panel noted that in all five cases the EEC prices were lower. The reported differences and corresponding EEC export refunds were as follows:

February 1980 (Sri Lanka)	-	\$34.09 - \$39.59	(refund \$105)
October 1980 (Yemen)	-	\$69.00	(refund \$91)
May 1981 (Yemen)	-	\$112.17	(refund \$67.80)
January 1982 (Jamaica)	-	\$36.83	(refund \$90.14)
February 1982 (Nigeria)	-	\$55.00	(refund \$87.00)

4.34 The Panel noted that for three particular markets only one specific transaction was presented in each case, and that while two cases were reported for Yemen, only one US price was quoted in each case. The Panel was aware of the difficulties in obtaining reliable information on actual pricing in wheat flour trade, but found that on the basis of the available information it had not sufficient ground to reach a definite conclusion as to whether price undercutting in the sense of Article 10:3 had occurred.

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<sup>1</sup>The Panel was of the opinion that the use of the years 1959/60 or 1963/64 as the starting year would not affect its findings.

<sup>2</sup>Chile, Israel, Nigeria, Philippines, Saudi Arabia (stronger position only in 1978/79 and largely

through IPT in 1979/80), Sierra Leone, Trinidad and Tobago, Zaire, Barbados.

<sup>3</sup>Egypt, Sri Lanka, Syria, Yemen, Lebanon, Jordan, Cameroon.

<sup>4</sup>The US also presented two cases from 1975 and 1976. As these cases predated the entry into force of obligations under Article 10:3, the Panel did not include them in its examination.

4.35 The Panel then examined the US argument that export unit values provided evidence of price undercutting. It considered that wheat flour was not a homogeneous product and that differences in qualities would lead to price differences.<sup>1</sup> It also considered that there was not reasonable price stability in the wheat flour market over a given period of time nor were there shipments of similar quantities by suppliers from the exporting countries under consideration. Consequently the Panel was of the opinion that these above characteristics of wheat flour market did not allow the use of report unit values in the particular case before it.

#### C. Nullification or Impairment; Serious Prejudice

4.36 The Panel considered the United States complaint that the application of EEC export refunds results in nullification or impairment to the United States, and is causing serious prejudice to the interests of the United States. The Panel found in its consideration that there is lack of clarity in the provisions of Article 8 as regards the demonstration of adverse effects in third countries markets so far as certain primary products are concerned. In light of the legal uncertainty in this regard the Panel did not find on nullification or impairment, or serious prejudice, beyond the question of adverse effects in terms of Article 10, dealt with in Sections A and B above.<sup>2</sup>

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<sup>1</sup>Wheat flour transactions are generally reported in foreign trade statistics under one heading

without distinction with respect to their quality.

<sup>2</sup>The Panel also took into account that in this case the United States complaint was largely based upon its contention that practices by the EEC were inconsistent with its obligations under Article 10, and that adverse effects were therefore pursuant to exist.

## V. Conclusions

The Panel reached the following conclusions:

5.1 EEC export refunds for wheat flour must be considered as a form of subsidy which was subject to the provisions of Article XVI of the General Agreement as interpreted and applied by the Code.

5.2 It was evident to the Panel that the EEC share of world exports of wheat flour has increased considerably over the period under consideration when application of EEC export subsidies was the general practice, while the share of the US and other suppliers has decreased.

5.3 The Panel found however that it was unable to conclude as to whether the increased share has resulted in the EEC "having more than an equitable share" in terms of Article 10, in light of the highly artificial levels and conditions of trade in wheat flour, the complexity of developments in the markets, including the interplay of a number of special factors, the relative importance of which it was impossible to assess, and, most importantly, the difficulties inherent in the concept of "more than equitable share".

5.4 The Panel concluded that, despite the considerable increase in EEC exports, market displacement in the sense of Article 10:2(a) was not evident in the seventeen markets examined by the Panel.

5.5 With regard to price undercutting in the sense of Article 10:3, the Panel found that, on the basis of available information there was not sufficient ground to reach a definite conclusion as to whether the EEC had granted export subsidies on export of wheat flour in a manner which resulted in prices materially below those of other suppliers to the same markets.

5.6 The Panel was not convinced, however, that the application of EEC export subsidies had not caused undue disturbance to the normal commercial interests of the United States in the sense of Article XVI:2, to the extent that it may well have resulted in reduced sales opportunities for the United States.

5.7 The Panel considered it desirable that the EEC, bearing in mind, the provisions of Article XVI:2, make greater efforts to limit the use of subsidies on the exports of wheat flour. The Panel considered that there were a number of practical aspects of the application of the export refund which might be examined to this end.

5.8 Finally, from a broader economic and trade policy perspective, the Panel considered the situation as regards export subsidies and other aspects of trade in wheat flour to be highly unsatisfactory and was concerned over what this implied for the effectiveness of the legal provisions in this area. The artificial level and conditions of much of the trade in this product typified the current problems and prospective risks. In this connection it found it anomalous, for instance, that the EEC which without the application of export subsidies would generally not be in a position to export substantial quantities of wheat flour, had over time increased its share of the world market to become by far the largest exporter.



5.9 The Panel considered that certain problems might be reduced by improved transparency and possibly other forms of multilateral co-operation in either the IWC or the GATT. It was of the view, however, that solutions to the problem of export subsidies in this area could only be found in making the pertinent provisions of the Code more operational, stringent and effective in application. Areas which deserve attention in this regard are, inter alia:

- (i) a clearer and common understanding of the concept of "more than equitable share", and rendering the concept more operational,
- (ii) consideration of whether international understandings relating to sales on other than commercial terms adequately complement and support intended disciplines on export subsidies.

ANNEX A

Changes in EEC Shipments to Individual Markets  
1980/1981 Compared to Previous Three-Year Average  
(1,000 metric ton wheat equivalent)

Markets where an increase of greater than 1,000 MT has taken place:		Markets where a decrease of greater than 1,000 MT has taken place:	
Malta	(+ 3.3)	Austria	(- 2.5)
USSR	(+ 661.5)	Barbados	(- 6.7)
Cuba	(+ 20.6)	Bolivia	(- 12.0)
Iraq	(+ 9.1)	Lebanon	(- 1.3)
Israel	(+ 3.3)	Saudi Arabia	(- 309.5)
Egypt	(+ 802.4)	Syria	(- 44.7)
Libya	(+ 117.0)	Pakistan	(- 3.4)
Poland	(+ 99.8)	Hong Kong	(- 1.0)
Jamaica	(+ 20.1)	Algeria	(- 48.6)
Yemen A. Rep.	(+ 28.5)	Kenya	(- 1.7)
Yemen P.D.R.	(+ 13.3)	Nigeria	(- 48.4)
Angola	(+ 76.3)	Iceland	(- 1.5)
Burundi	(+ 1.6)	Romania	(- 1.9)
Cameroon	(+ 32.9)	Mexico	(- 1.5)
Central African Rep.	(+ 2.6)	West Indies	(- 4.2)
Comoro	(+ 2.8)	Chile	(- 19.7)
Gambia	(+ 3.8)	Cyprus	(- 1.5)
Guinea	(+ 5.5)	Jordan	(- 19.2)
G. Bissau	(+ 1.1)	Oman	(- 7.1)
Madagascar	(+ 2.1)	UAE	(- 5.5)
Mali	(+ 16.6)	Burma	(- 1.7)
Mauritania	(+ 5.3)	Philippines	(- 5.1)
Mozambique	(+ 3.2)	Sri Lanka	(- 362.2)
Sierra Leone	(+ 12.3)	Vietnam	(- 104.4)
Tanzania	(+ 8.8)	Burundi	(- 1.6)
Zaire	(+ 4.1)	Congo	(- 11.7)
		Eq. Guinea	(- 2.6)
		Ethiopia	(- 8.8)
		Gabon	(- 1.6)
		Ghana	(- 7.2)
		Liberia	(- 1.2)
		Malawi	(- 1.4)
		Niger	(- 1.9)
		Sao Tomé	(- 2.6)
		Senegal	(- 3.9)
		Somalia	(- 5.5)
		New Caledonia	(- 1.1)

Source: IWC Record of Operations

## ANNEX B

1. There are a number of problems in establishing price levels on the international wheat flour market. There is no recognized world price, there is lack of transparency in international wheat flour sales generally, and there are relatively low levels of wheat flour of a quality comparable to the EEC standard product exported by other suppliers to provide a consistently reliable export price standard.
2. The EEC constructs a world price for wheat flour drawing on the following sources:
  - (a) quotations for wheat of a roughly comparable quality to EEC wheat, such as US "Soft Red Winter, FOB Gulf";
  - (b) prices of wheat from the US or other sources delivered to Rotterdam;
  - (c) prices actually prevailing on various markets for competing flour, to the extent these are known;
  - (d) prices of US flour as reported in the US milling trade periodical Milling and Baking News (normally hard flour prices, adjusted downward to take into account quality differences).
3. There are difficulties inherent in drawing from each of these sources:
  - (a) US "Soft Red Winter, FOB Gulf" - prices obtained on the wheat market for SRW are not absolutely consistent with EEC common wheat; a calculation must be made to transform the wheat price to a flour price; and SRW based wheat flour is not marketed in quantities internationally or with sufficient price transparency to provide a consistently valid price comparison;
  - (b) wheat imported through Rotterdam - this is seldom of quality comparable to EEC wheat, and comparison is difficult given that prices are established according to the different qualities and properties of flour;
  - (c) prevailing market prices - these are seldom adequate, because of lack of established market prices as in certain other commodities, trade confidentiality, and delays in information in those instances where contract awards are published. Since these price reports are so varied, it is difficult to assess how representative they are;
  - (d) US price quotations from US trade journals - these prices primarily reflect the US market and not the real world market, given the relative importance and structure of US flour exports.

In the final analysis, judgements must be made on such information to arrive at what is considered to be an appropriate export refund. An overriding consideration remains the world price of wheat, and the fact that if flour prices were fixed at unduly high levels in relation to wheat, it would tend to further the trend toward domestic milling capacity, thereby reducing the international trade in wheat flour.

ANNEX C

Exports of Wheat Flour to Selected Markets -  
Tables submitted by the United States in connection with  
its representation under Article 10:2

[See original document - tables pp.45 - 77]