

***BRAZIL – EXPORT FINANCING PROGRAMME FOR
AIRCRAFT***

REPORT OF THE PANEL

The report of the Panel on *Brazil – Export Financing Programme for Aircraft* is being circulated to all Members, pursuant to the DSU. The report is being circulated as an unrestricted document from 14 April 1999, pursuant to the Procedures for the Circulation and Derestriction of WTO Documents (WT/L/160/Rev.1). Members are reminded that, in accordance with the DSU, only parties to the dispute may appeal a panel report. An appeal shall be limited to issues of law covered in the Panel report and legal interpretations developed by the Panel. There shall be no *ex parte* communications with the Panel or Appellate Body concerning matters under consideration by the Panel or Appellate Body.

Note by the Secretariat: This Panel Report shall be adopted by the Dispute Settlement Body (DSB) within 30 days after the date of its circulation unless a party to the dispute decides to appeal or the DSB decides by consensus not to adopt the report. If the Panel Report is appealed to the Appellate Body, it shall not be considered for adoption by the DSB until after the completion of the appeal. Information on the current status of the Panel Report is available from the WTO Secretariat.

I. INTRODUCTION

1.1 On 18 June 1996, Canada requested consultations with Brazil under Article 4 of the Agreement on Subsidies and Countervailing Measures ("SCM Agreement") and Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"), regarding "certain export subsidies granted under the Brazilian Programa de Financiamento as Exportações ("PROEX") to foreign purchasers of Brazil's EMBRAER aircraft."¹

1.2 Canada and Brazil held consultations on 22 and 25 July 1996 in Geneva, but failed to reach a mutually satisfactory solution. On 16 September 1996, Canada requested the establishment of a panel under Articles 4 and 30 of the SCM Agreement and Articles 4 and 6 of the DSU.² In a communication dated 23 September 1996 and addressed to the Dispute Settlement Body ("DSB"), Brazil reserved its rights to invoke Article 27 of the SCM Agreement before any panel that was established to examine the matter at issue, and requested that the terms of reference proposed by Canada explicitly recognize Brazil's right to do so.

1.3 On 3 October 1996, Canada again requested the establishment of a panel.³ That request was subsequently withdrawn to allow the parties to seek a mutually satisfactory solution to the problem.

1.4 On 10 July 1998, Canada again requested the establishment of a panel under Article 4 of the SCM Agreement.

1.5 At its meeting on 23 July 1998, the Dispute Settlement Body ("DSB") established a Panel in accordance with Article 4 of the SCM Agreement with the following standard terms of reference:

"To examine, in the light of the relevant provisions of the SCM Agreement, the matter referred to the DSB by Canada in document WT/DS46/5 and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in that agreement."⁴

1.6 The European Communities ("EC") and the United States ("US") reserved their rights to participate in the panel proceedings as third parties.⁵

1.7 On 16 October 1998, Canada requested the Director-General of the WTO to determine the composition of the Panel, pursuant to Article 8.7 of the DSU. On 22 October 1998, the Director-General composed the Panel as follows:

Chairman: Mr. Dariusz Rosati
Members: Professor Akio Shimizu
Mr. Kajit Sukhum

1.8 The Panel met with the parties on 23/24 November 1998 and 14 December 1998. It met with the third parties on 24 November 1998.

1.9 The Panel submitted its interim report to the parties on 17 February 1999. On 25 February 1999 both parties submitted written requests for the Panel to review precise aspects of the interim report, and

¹See Canada's request for consultations, WT/DS46/1.

²WT/DS46/5; 13 July 1998.

³WT/DS46/4; 4 October 1996.

⁴WT/DS46/7; 28 October 1998.

⁵WT/DS46/6; 19 August 1998.

on 3 March 1999 each party submitted written comments regarding the other's request. Neither party requested a further meeting with the Panel. The Panel submitted its final report to the parties on 12 March 1999.

1.10 Given the nature of the dispute, and with the agreement of the parties, special procedures were created by the Panel for handling business confidential information. The special procedures are found in Annex 1 to this report. Under paragraph VII:2 of these procedures, "[t]he Panel shall not disclose Business Confidential Information in its interim and final reports, but may make statements of conclusion drawn from such information." Thus, where Business Confidential Information had been submitted by a party in support of a claim, it is mentioned in the report, but details of such information are not disclosed.

II. FACTUAL ASPECTS

2.1 This dispute concerns payments under the interest rate equalization component of the Programa de Financiamento as Exportações ("PROEX"), the export financing support programme of Brazil, on exports of Brazilian regional aircraft. PROEX was created by the Government of Brazil on 1 June 1991 by Law No. 8187/91 and is currently being maintained by provisional measures issued by the Brazilian government on a monthly basis.⁶ PROEX provides export credits to Brazilian exporters either through direct financing or interest rate equalization payments.⁷

2.2 With direct financing, Brazil lends a portion of the funds required for the transaction. With interest equalization, underlying legal instruments provide that the "National Treasury grant[s] to the financing party an equalization payment to cover, at most, the difference between the interest charges contracted with the buyer and the cost to the financing party of raising the required funds."⁸

2.3 The financing terms for which interest rate equalization payments are made are set by Ministerial Decrees. The terms, determined by the product to be exported, vary normally from one year to ten years. In the case of regional aircraft, however, this term has been extended to 15 years. The length of the financing term, in turn, determines the spread to be equalised: the payment ranges from 2 percentage points per annum, up to 3.8 percentage points per annum for a term of nine years or more.⁹ The spread is fixed and does not vary depending on the lender's actual cost of funds.¹⁰

2.4 PROEX is administered by the Comitê de Crédito as Exportações ("Committee"), a 13-agency group, with the Ministry of Finance serving as its executive. Day-to-day operations of PROEX are conducted by the Banco do Brasil. For applications for financing transactions not exceeding US\$5 million, whose terms otherwise fall within PROEX guidelines, Banco do Brasil has pre-approved authority to provide PROEX support without requesting the approval of the Committee. All other applications are referred to the Committee, which has the authority to waive some of the published PROEX guidelines. In the case of regional jet aircraft, the most frequent waiver has been to extend the length of the financing term from ten to fifteen years.

⁶As of the date of the request for the establishment of a panel, the relevant legal instrument was Provisional Measure 1700/15 of 30 June 1998. It replaced Provisional Measure 1629-13 of 12 February 1998, which had replaced the basic law establishing PROEX, Law No. 8.187 of 1 June 1991, as amended by Resolution 2380 of 25 April 1997.

⁷Law No. 8.187, 1 June 1991 (Exhibit Bra-3), replaced by Provisional Measure No. 1629, 12 February 1998 (Exhibit Bra-4).

⁸See, for example, Resolution 2380/97 of 25 April 1997.

⁹See Central Bank of Brazil Circular Letter number 2.601 dated 29 November 1995. Prior to that date, the spread to be equalised for financing for a term of nine years or more was 3.5 percentage points.

¹⁰Evaluation of the Brazilian Export Program ("Finan Report") p. 2.7.

2.5 PROEX involvement in aircraft financing transactions begins when the manufacturer requests a letter of approval from the Committee prior to conclusion of a formal agreement with the buyer. This request sets forth the terms and conditions of the proposed transaction. If the Committee approves, it issues a letter of commitment to the manufacturer. This letter commits PROEX to providing support as specified for the transaction provided that the contract is entered into according to the terms and conditions contained in the request for approval, and provided that it is entered into within a specified period of time, usually 90 days. If a contract is not entered into within the specified time, the commitment contained in the letter of approval expires.

2.6 PROEX interest equalization payments, pursuant to the commitment, begin after the aircraft is exported and paid for by the purchaser. PROEX payments are made to the lending financial institution in the form of non-interest bearing National Treasury Bonds (Notas do Tesouro Nacional – Série I) referred to as NTN-I bonds. These are denominated in Brazilian Reais indexed to the United States dollar. The bonds are issued by the Brazilian National Treasury to its agent bank, Banco do Brasil, which then passes them on to the lending banks financing the transaction. The bonds are issued in the name of the lending bank which can decide to redeem them on a semi-annual basis for the duration of the financing or discount them for a lump sum in the market. PROEX resembles a series of zero coupon bonds which mature at six months intervals over the course of the financing period. The bonds can only be redeemed in Brazil and only in Brazilian currency at the exchange rate prevailing at the time of payment. If the lending bank is outside of Brazil, it may appoint a Brazilian bank as its agent to receive the semi-annual payments on its behalf.

III. FINDINGS AND RECOMMENDATIONS REQUESTED BY THE PARTIES

A. FINDINGS OF FACT

3.1 **Canada** requests the Panel to make the following findings of fact:

- (a) That PROEX interest equalization payments are made in the form of instalments or lump sums.
- (b) That PROEX interest equalization payments have been made in respect of the following transactions: (a) Brasilia 120 model (Skywest, Great Lakes Airlines; Rio Sul and other unspecified transactions); (b) ERJ-145 model (American Eagle; British Regional; Portugalia; Regional; Rio Sul; Siv Am; Wexford; Continental Express (“COEX”); Trans States; Luxair; City Airlines; and other unspecified transactions).
- (c) That the level of PROEX and BEFIEX expenditures has increased since 1 January 1995 and, as a result, the level of Brazilian export subsidies has increased since that date.
- (d) That PROEX and BEFIEX, and therefore Brazilian export subsidies, are not being phased out by 31 December 2002.

B. FINDINGS OF LAW

3.2 **Canada** requests the Panel to make the following findings of law:

- (a) That, as admitted by Brazil, PROEX interest equalization payments are export subsidies within the meaning of Article 3 of the SCM Agreement.

(b) That, more specifically, but without foregoing the generality of the previous finding, PROEX interest equalization payments made in respect of the following transactions are prohibited export subsidies: (a) Brasilia 120 model (Skywest, Great Lakes Airlines; Rio Sul and other unspecified transactions); (b) ERJ-145 model (American Eagle; British Regional; Portugalia; Regional; Rio Sul; Siv Am; Wexford; Continental Express (“COEX”); Trans States; Luxair; City Airlines; and other unspecified transactions).

(c) That the first paragraph of Item (k) of Annex 1 of the SCM Agreement does not provide an exception to Article 3.

(d) That, even if the first paragraph of Item (k) does provide, through an a contrario inference such an exception, PROEX interest equalization payments are not payments within the meaning of Item (k), or do provide a material advantage in the field of export credit terms, and as such do not fall within the exception.

(e) That Brazil does not meet the conditions set out in Article 27.4 and that, as a result, it does not benefit from the eight year grace period from the general prohibition on export subsidies in Article 3, provided for developing countries under Article 27.2(b).

C. RECOMMENDATIONS

3.3 In its first written submission to the Panel, **Canada** requested the Panel to make the following recommendations:

- (a) "Brazil shall not grant new subsidies under PROEX, including subsidies promised or committed, but not yet granted, on regional aircraft not yet delivered";
- (b) "Brazil shall no longer maintain existing subsidies under PROEX and must terminate such subsidies no later than three months after the adoption of the Report of the Panel by the DSB"; and
- (c) "Brazil shall withdraw without delay PROEX subsidies granted pursuant to transactions entered into following the composition of the Panel on October 22, 1998."

In its second oral submission to the Panel, **Canada** further requested the Panel to make the following recommendations:

- (d) That, if the Panel finds that PROEX interest equalization export subsidies are granted on an instalment basis at the time of the periodic payment of the subsidies, the Panel recommend that such payments be terminated no later than 3 months after the date of the adoption of the Panel's Report by the Dispute Settlement Body, in respect of aircraft that have already been delivered or in respect of any aircraft delivered after that date.
- (e) That, if the Panel finds that PROEX subsidies are granted at the time of the delivery of the aircraft, the Panel recommend that no such subsidies be granted in respect of any aircraft delivered after the date of the adoption of the Panel's Report by the DSB.
- (f) That the Panel recommend that any PROEX interest equalization export subsidies paid or granted in respect of any new orders of aircraft between the date of the composition of the Panel on October 22, 1998 and the date that the Panel Report is adopted by the DSB

be withdrawn as prohibited export subsidies intended to circumvent the Panel's recommendations.

3.4 **Brazil** requests the Panel to find that "PROEX is not inconsistent with Brazil's obligations under Article 3 of the Agreement on Subsidies and Countervailing Measures."

[Parties' arguments in Sections IV and V deleted from this version]

VI. INTERIM REVIEW

6.1 On 25 February 1999 both parties submitted written requests for the Panel to review precise aspects of the interim report, and on 3 March 1999 each party submitted written comments regarding the other's request. Neither party requested a further meeting with the Panel.

6.2 Canada notes that, in paragraph 7.18 and in footnotes 194 and 195 of the interim report (footnotes 197 and 198 of this report), we considered but failed to make findings on two legal issues related to Brazil's affirmative defense based on the first paragraph of item (k) of the Illustrative List of Export Subsidies. In Canada's view, the principle of judicial economy does not properly apply to these issues, and the Panel should have resolved them. Canada states that, as the Appellate Body observed in *Australia – Salmon*¹⁸⁰, the aim of dispute settlement, according to Article 3.7 of the DSU, is to "secure a positive solution to the dispute." Accordingly,

"A Panel has to address those claims on which a finding is necessary in order to enable the DSB to make sufficiently precise recommendations and rulings so as to allow for prompt compliance by a Member with those recommendations and rulings...."¹⁸¹

6.3 Canada contends that Brazil has argued that the first paragraph of item (k) is an exception that provides cover for PROEX payments. As it stands, the Interim Report concludes that PROEX, an admitted export subsidy, is applied in such a way that it would not benefit from the "material advantage" clause of this item. The import of the Panel's findings is that Brazil could not bring PROEX payments into compliance by, for example, simply adjusting the *rate* of subsidization and then arguing that these payments no longer "secure a material advantage". Canada considers that the Panel should give this point greater precision by finding that the first paragraph of item (k) cannot be used as an exception at all, and that in any event, PROEX payments are not "payments" within the meaning of item (k).

6.4 In paragraph 7.18 of our interim report, we found that Brazil's "material advantage" defense under the first paragraph of item (k) could succeed only if Brazil prevailed on three legal issues. We concluded that PROEX payments were "used to secure a material advantage in the field of export credit terms", and declined to reach the other two legal issues presented with respect to that defense. In considering Canada's argument that we should address the remaining legal issues, we note that, in *Australia – Salmon*, the Appellate Body addressed the circumstances under which a panel might or might not address certain *claims* raised by a complainant. In this case, however, the question is whether we should have reached all legal *issues* related to a particular claim. In any event, Canada has not convinced us that, in this case, deciding the remaining legal issues would provide any further guidance with respect to compliance with the recommendations and rulings of the DSB. Thus, recalling that the purpose of the dispute settlement process is to "secure a positive solution to the dispute", and because in our view issues of legal interpretation are best addressed in concrete cases where they are necessary to resolve the case at hand, we decline to take up Canada's invitation to resolve the two legal issues in question.

6.5 Brazil argues that the appropriate time-period to withdraw the subsidy noted in paragraph 8.5 of the Report should be seven and one-half months. In Brazil's view, since Article 4.7 of the SCM Agreement does not specify a specific time-period, the time-period set forth in Article 21.3(c) of the DSU should be halved pursuant to Article 4.12 of the SCM Agreement. Brazil further contends that no evidence has been presented in this case to justify departing from the seven and one-half month guideline.

¹⁸⁰ *Australia – Measures Affecting the Importation of Salmon*, WT/DS18/AB/R, Report of the Appellate Body adopted on 6 November 1998.

¹⁸¹ *Id.*, para. 223.

Brazil further notes that PROEX was created by the Brazilian Congress, and that any changes therefore must also be enacted by Congress. It is therefore impracticable for Brazil to comply with the Panel's recommendation within 90 days. Finally, Brazil noted that the world financial crisis had had a significant and detrimental effect on Brazil. Brazil noted that, in *Indonesia – Autos*, the arbitrator allocated Indonesia an additional period of six months over and above the time required for the completion of its domestic rule-making process pursuant to Article 21.2 of the DSU.¹⁸²

6.6 Canada responds that, at issue in this dispute is not the PROEX programme *as such*, but the way that programme is *applied* to the export sales of regional aircraft. Brazil can comply with the recommendation of the Panel simply by stopping the payment of such subsidies on exported regional aircraft delivered after the date of adoption of the Panel Report. Because neither the annulled PROEX legislation nor the monthly Presidential decrees that currently maintain the programme are mandatory, there is no legal requirement for Congressional action before the payment of PROEX export subsidies – that is, the issuance of NTN-1 bonds – on the delivery of exported aircraft is stopped. Canada further argues that Article 4.12 applies only to the "conduct of such disputes", not to implementation, and that the "reasonable period of time" standard set forth in Article 21.3(c) is not the benchmark of "without delay" for the purposes of Article 4.7 of the SCM Agreement. Finally, Canada argues that it is not apparent how Brazil's mention of its status as a developing country Member or mention of its current financial crisis in any way affects the period of time for compliance with the Panel's recommendation.

6.7 We decline Brazil's request to modify the time-period set forth in paragraph 8.5. Assuming that the time-period set forth in Article 21.3(c) of the DSU, as halved pursuant to Article 4.12 of the SCM Agreement, is applicable to disputes under Article 4 of the SCM Agreement -- an issue we do not decide -- Article 21.3(c) of the DSU merely states that the "reasonable period of time" to implement panel or Appellate Body recommendations "should not exceed" 15 months. In this case, and reading that provision in conjunction with the requirement of Article 4.7 that the subsidy be withdrawn "without delay", we do not consider that a seven and one-half month time-period would be appropriate. We note that, while PROEX was created by legislation, it is currently maintained in force through Provisional Measures issued by the Brazilian government on a monthly basis. In any event, we recall Canada's view that implementation does not in the first instance require the modification of the PROEX interest rate equalization scheme itself, but merely a cessation in the issuance of new bonds upon exportation of Brazilian regional aircraft. Nor do we consider that, in the particular circumstances of this case, Article 21.2 of the DSU would warrant stretching the ordinary meaning of the phrase "without delay" to provide for an implementation period of seven and one-half months. Accordingly, we have not modified the time-period specified for withdrawal of the measure.

6.8 Canada states that it is implicit in our findings and conclusions that all of the conditions of Article 27 have to be met before a developing country Member may benefit from Article 27, and asks that we state this explicitly. We have modified paragraphs 7.57 and 8.1(c) in response to Canada's request. We have also clarified our findings through modifications to paragraphs 8.1(a), 8.1(b) and footnote 198. Finally, we have made other minor modifications of a typographical nature, including those in paragraphs 7.13, 7.30, 7.34, 7.53, 7.56, 7.68, 7.71, 7.72, 7.73, 7.75 and footnotes 198, 200, 215, 220, 231, and 241.

¹⁸² *Indonesia – Certain Measures Affecting the Automobile Industry*, Award of the Arbitrator, WT/DS64/15, WT/DS55/14, WT/DS59/13, WT/DS64/12, para. 24.

VII. FINDINGS

A. THE MEASURES AT ISSUE

7.1. In its request for establishment of a panel (WT/DS46/5), Canada asks that the Panel "consider and find that export subsidies under PROEX are inconsistent with Article 3 of the SCM Agreement." In its first submission to the Panel, Canada clarifies that "[a]t issue in this dispute is whether the *Programa de Financiamento às Exportações* (PROEX) . . . confers export subsidies on sales of Brazilian regional aircraft that are prohibited under Article 3 of the . . . SCM Agreement"¹⁸³, and asks the Panel to find that "payments made under the 'Interest Equalization' component of PROEX on exported Brazilian regional aircraft" constitute prohibited subsidies.¹⁸⁴ In its second submission, Canada states that "the 'matter' subject to its request for a Panel was PROEX and the export subsidies paid under that programme to civil aircraft. This was the same 'prohibited subsidy' on which Canada had requested consultations."¹⁸⁵ A few paragraphs later, Canada states that "it is Canada's submission that export subsidies paid under PROEX, the Brazilian export subsidy programme, on all exported Brazilian regional aircraft, in whatever amount and regardless of the specific legislative instrument that underlies the programme, are prohibited by Article 3 and must be withdrawn. It is this practice that is the subject of Canada's challenge."¹⁸⁶

7.2. We note that there is a certain lack of clarity regarding the precise measures being challenged by Canada. We do not understand Canada to be alleging that the interest rate equalization component of the PROEX programme *per se* is the prohibited measure, because Canada does not seek a finding or recommendation with respect to the programme itself.¹⁸⁷ In fact, it limits itself to challenging PROEX payments relating to the particular sector of regional aircraft.¹⁸⁸ On the other hand, neither is Canada restricting its challenge to a particular specified payment or payments already made pursuant to the interest rate equalization component of PROEX. To the contrary, although Canada identifies specific transactions with respect to which it considers that PROEX payments have been or will be made, Canada is arguing that all PROEX payments, to the extent they relate to exported Brazilian regional aircraft, *including payments to be made in the future pursuant to the PROEX interest rate equalization scheme*, are prohibited subsidies. Thus, we understand Canada to be challenging not only specific payments, but more generally the practice involving PROEX payments relating to exported Brazilian regional aircraft (which we will hereafter refer to as "PROEX payments"). In order to analyse this contention, we are required to go beyond an examination of individual PROEX payments that have been identified and look

¹⁸³ Canada first submission, paragraph 1.

¹⁸⁴ Canada first submission, paragraph 2. Although Canada's request for establishment of a panel also identifies "export financing under PROEX", i.e., PROEX direct export financing, Canada states that it "does not challenge PROEX Financing in this dispute." Canada first submission, paragraph 30.

¹⁸⁵ Canada second submission, paragraph 19.

¹⁸⁶ Canada second submission, paragraph 23.

¹⁸⁷ Because we understand that Canada has not challenged the PROEX programme *per se*, we need not address the issue whether the PROEX programme may be subject to challenge under Article 4 of the SCM Agreement. We note however that in our view the effective operation of the SCM Agreement requires that a party be able in some manner to obtain prospective discipline on the provision of subsidies in cases where it can be established in advance, based upon the legal framework governing the provision of those subsidies, that they would be inconsistent with Article 3 of the SCM Agreement. Otherwise, the SCM Agreement's prohibitions could not be invoked until a particular prohibited subsidy had actually been paid. This would be tantamount to the proverbial closing of the barn door after the cows have gone.

¹⁸⁸ In its request for findings, Canada sometimes refers to "civil aircraft" and at other times refers to "regional aircraft". Judging from the totality of Canada's submissions, however, we conclude that Canada is challenging PROEX interest rate equalization payments only with respect to regional aircraft. Canada defines the regional aircraft market as consisting of commercial aircraft with 20-90 seats, whether turboprop or jet. On the basis of the evidence before us, it appears that three EMBRAER aircraft --the ERJ-145, the ERJ-135 and the EMB-120 -- fall within this definition.

more generally at the nature and operation of the PROEX interest rate equalization scheme which governs the payment of the alleged export subsidies.¹⁸⁹

7.3. Because Canada is challenging not only specific PROEX payments relating to regional aircraft, but more generally the practice of providing PROEX payments, we do not and could not have before us a comprehensive list of the transactions supported by PROEX interest rate equalization which are challenged by Canada. We note however that Brazil has provided a list of post 1 January 1995 transactions supported by PROEX interest rate equalization relating to two Brazilian regional aircraft, the EMB-120 and the ERJ-145, and Canada has requested that we make specific findings regarding PROEX payments relating to these transactions. The transactions relating to the EMB-120 involve Great Lakes Airlines, Rio Sul, Skywest and "others", while those relating to the ERJ-145 involve American Eagle, British Regional, City Airlines, Continental Express, Luxair, Portugalia, Regional, Rio Sul, Siv Am, Trans States, Wexford and "other". Thus, the payments subject to challenge in this dispute include, but are not limited to, PROEX payments made or to be made with respect to the transactions identified above.

B. PRELIMINARY OBJECTION BY BRAZIL

7.4. Canada's request for establishment of a panel (WT/DS46/5) contains a list of provisional measures, laws, decrees and other legal instruments which govern the operation of the PROEX programme. Brazil objects to the Panel's consideration of certain of these "measures" on the grounds that they were enacted or implemented subsequent to the last consultations between the parties and, as a result, were not and could not have been the subject of consultations. Brazil contends that Article 6.2 of the DSU requires that consultations with respect to the specific measures at issue must have taken place in order for a measure to be within a panel's terms of reference. Brazil further argues that Article 4 of the DSU requires that parties consult regarding a matter before resorting to a panel with respect to that matter.

7.5. Canada acknowledges that the legal instruments in question did not exist at the time consultations were held and thus were not themselves the subject of consultations. It contends, however, that the "matter" referred to in Canada's request for establishment of a panel – the payment of export subsidies under PROEX – was the same prohibited subsidy with respect to which the parties held consultations, in the sense that that matter is directly connected to the prohibited subsidy subject to the consultations and flows directly from it. Canada further notes that the Provisional Measure underlying PROEX must be renewed every month, and that Brazil's argument, if accepted, would bar examination of PROEX by a WTO dispute settlement panel altogether.

7.6. The objections raised by Brazil present us with an issue regarding the relationship between the matter before a panel as defined by its terms of reference and the matter consulted upon. Specifically, we must consider whether and to what extent a panel is limited in its consideration of the matter identified in its terms of reference by the scope of the matter with respect to which consultations were held. In considering this question in this dispute, we must apply not only the relevant provisions of the DSU, but also the special or additional dispute settlement provisions found in Article 4.2 through 4.12 of the SCM Agreement, keeping in mind the injunction of Article 1.2 of the DSU that, "[t]o the extent there is a difference between the rules and procedures of the [DSU] and the special or additional rules and

¹⁸⁹ As discussed in the following section of these findings, there are a wide range of legislative and regulatory instruments which collectively govern the operation of the PROEX programme. As these provisions have changed over time, certain aspects of the operation of PROEX interest rate equalization have also changed. In assessing the consistency of PROEX payments with the SCM Agreement, we will examine the operation of the regime up to and as of the date of the request for establishment of a panel by Canada.

procedures set forth in Appendix 2, the special or additional rules and procedures in Appendix 2 shall prevail."

7.7. In examining this issue, we first recall that our terms of reference are the standard terms of reference provided for in Article 7.1 of the DSU. Under those terms of reference, we are required to examine the "matter referred to the DSB" by Canada in its request for establishment (WT/DS46/5). As the Appellate Body explained in *Guatemala – Anti-Dumping Investigation Regarding Portland Cement from Mexico*¹⁹⁰ "the 'matter referred to the DSB', therefore, consists of two elements: the specific measures at issue and the legal basis of the complaint (or the claims)"(emphasis in original). The Appellate Body derived the meaning of the term "matter" in Article 7 of the DSU from Article 6.2 of the DSU, which requires that a request for establishment of a panel "identify the specific measures at issue and provide a brief summary of the legal basis of the complaint..." In this case, the measures alleged by Canada in its request for establishment of a panel to be inconsistent with the SCM Agreement are "export subsidies under PROEX." Thus, although Canada in its request for establishment of a panel identifies a list of legal instruments which it refers to as "measures", Canada is not, in our view, alleging that each of these legal instruments separately represents a measure inconsistent with Article 3 of the SCM Agreement. Rather, the legal instruments identified by Canada taken collectively represent a list of legal instruments relating to the payment of the alleged export subsidies under the PROEX scheme.

7.8. Turning next to Canada's request for consultations, we note that Article 4.4 of the DSU requires that a request for consultations "give the reasons for the request, including identification of the measures at issue and an indication of the legal basis for the complaint." Article 4.2 of the SCM Agreement requires a statement of available evidence with regard to "the existence and nature of the subsidy in question" and Article 4.3 of the SCM Agreement requires the Member "granting or maintaining the subsidy in question" to enter into consultations as quickly as possible. In this case, Canada requested consultations "regarding certain export subsidies granted under the Brazilian *Programa de Financiamento às Exportações* (PROEX) to foreign purchasers of Brazil's EMBRAER aircraft." Thus, it is clear to us that the request for consultations related to the same general subject as the request for establishment of a panel, i.e., "export subsidies under PROEX". The request for consultations does not, however, identify the particular legal instruments which Brazil contends that we should not consider, nor could it have, because those particular legal instruments did not exist at the time the request for consultations was made. In fact, it is clear that the PROEX regime (and thus potentially the attributes of the PROEX payments under it) has changed over time, and that between the date the last consultations were held and the date that establishment of a panel was requested, some such changes occurred.

7.9. We recall that our terms of reference are based upon Canada's request for establishment of a panel, and not upon Canada's request for consultations. These terms of reference were established by the DSB pursuant to Article 7.1 of the DSU and establish the parameters for our work.¹⁹¹ Nothing in the text of the DSU or Article 4 of the SCM Agreement provides that the scope of a panel's work is governed by the scope of prior consultations. Nor do we consider that we should seek to somehow imply such a requirement into the WTO Agreement. One purpose of consultations, as set forth in Article 4.3 of the SCM Agreement, is to "clarify the facts of the situation",¹⁹² and it can be expected that information obtained during the course of consultations may enable the complainant to focus the scope of the matter

¹⁹⁰ Adopted 25 November 1998, WT/DS60/AB/R, para. 72.

¹⁹¹ See, e.g., *India – Patent Protection for Pharmaceutical and Agricultural Chemical Products*, adopted 16 January 1998, WT/DS50/AB/R, para. 92 ("The jurisdiction of a panel is established by that Panel's terms of reference, which are governed by Article 7 of the DSU.").

¹⁹² As the Appellate Body has noted, "the claims that are made and the facts that are established during consultations do much to shape the substance and the scope of subsequent panel proceedings." *India – Patent Protection for Pharmaceutical and Agricultural Chemical Products*, adopted 16 January 1998, WT/DS50/AB/R, para. 94.

with respect to which it seeks establishment of a panel. Thus, to limit the scope of the panel proceedings to the identical matter with respect to which consultations were held could undermine the effectiveness of the panel process.

7.10. We do not believe, however, that the question of consultations is completely outside our consideration. A party is not entitled to request establishment of a panel unless consultations have been held. Specifically, Article 4.7 of the DSU provides that a complaining party may request establishment of a panel only if "consultations fail to settle a dispute". Similarly, Article 4.4 of the SCM Agreement allows a "matter" to be referred to the DSB for establishment of a panel only if consultations have failed to lead to a mutually agreed solution. Given that Article 6.1 of the DSU and Article 4.4 of the SCM Agreement essentially require the DSB to establish a panel automatically upon request of a party, a panel cannot rely upon the DSB to ascertain that requisite consultations have been held and to establish a panel only in those cases.¹⁹³ Accordingly, we consider that a panel may consider whether consultations have been held with respect to a "dispute", and that a preliminary objection may properly be sustained if a party can establish that the required consultations had not been held with respect to a dispute. We do not believe, however, that either Article 4.7 of the DSU or Article 4.4 of the SCM Agreement requires a precise identity between the matter with respect to which consultations were held and that with respect to which establishment of a panel was requested.

7.11. Applying this analysis to the case at hand, we recall that Brazil and Canada consulted "regarding certain export subsidies granted under the Brazilian *Programa de Financiamento às Exportações* (PROEX) to foreign purchasers of Brazil's EMBRAER aircraft", and that the request for establishment of a panel relates to "export subsidies under PROEX". We consider that the consultations and request for establishment relate to what is fundamentally the same "dispute", because they involve essentially the same practice, i.e., the payment of export subsidies under PROEX. Under these circumstances, and notwithstanding the fact that both the authorizing legal instrument and certain other legal instruments relating to the administration of the PROEX interest equalization regime changed or were only introduced subsequent to the last consultations, we cannot say that Canada has failed to comply with the requirements of Article 4.7 of the DSU. Accordingly, the preliminary objection of Brazil is denied.

C. ARE PROEX INTEREST RATE EQUALIZATION PAYMENTS EXPORT SUBSIDIES?

7.12. Canada argues that PROEX payments are subsidies within the meaning of Article 1 of the SCM Agreement which are contingent upon export performance within the meaning of Article 3.1(a) of that Agreement. Specifically, Canada contends that PROEX payments are financial contributions in the form either of a direct transfer of funds (a grant) within the meaning of Article 1.1(a)(1)(i) or an "indirect financial contribution" through a funding mechanism or a private body in the sense of Article 1.1(a)(1)(iv) of the SCM Agreement. Canada further contends that this "financial contribution" confers a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement in as much as it reduces the interest rate paid by purchasers of exported Brazilian regional aircraft by up to 3.8 percentage points. Finally, Canada asserts that PROEX payments are contingent upon export performance within the meaning of Article 3.1(a) of the SCM Agreement in as much as they are available only with respect to the financing

¹⁹³ As stated by the Appellate Body in a somewhat different context in *European Communities – Regime for the Importation, Sale and Distribution of Bananas*, adopted 25 September 1997, WT/DS27/AB/R, para. 142:

"We recognize that a panel request will usually be approved automatically at the DSB meeting following the meeting at which the request first appears on the DSB's agenda. As a panel request is normally not subjected to detailed scrutiny by the DSB, it is incumbent upon a panel to examine the request for the establishment of the panel carefully to ensure its compliance with both the letter and the spirit of Article 6.2 of the DSU."

of export shipments. In its first submission, Brazil stated that it "does not dispute the assertion that PROEX interest equalization payments for aircraft constitute an export subsidy."¹⁹⁴ In response to a question from the Panel, Brazil reaffirmed that it "has not denied that PROEX interest rate equalization payments for aircraft fulfill the definition of a subsidy within the meaning of Article 1 and are contingent upon export within the meaning of Article 3.1(a)."¹⁹⁵

7.13. As noted above, the parties agree that PROEX payments are subsidies within the meaning of Article 1 of the SCM Agreement which are contingent upon exportation within the meaning of Article 3.1(a) of the Agreement, and we agree with them. Although the parties disagree about the form of the financial contribution involved – with Canada arguing that they involve a direct transfer of funds, and Brazil adopting the European Communities' view that they also involve a potential direct transfer of funds provided at an earlier moment in time – we consider that the issue presented relates to the question as to when the subsidies in question are paid and not as to whether they exist. We note that, according to Article 1:1(i) a subsidy exists if a government practice involves a direct transfer of funds or a potential direct transfer of funds and not only when a government actually effectuates such a transfer or potential transfer (otherwise the text of (i) would read: "a government directly transfers funds ... or engages in potential direct transfers of funds or liabilities"). The PROEX interest rate equalization scheme for aircraft fulfils the definition of a subsidy because there is a government practice, whether it involves a direct transfer of funds -- as Canada believes -- or a potential direct transfer of funds – as Brazil believes. As soon as there is such a practice, a subsidy exists, and the question whether the practice involves a direct transfer of funds or a potential direct transfer of funds is not relevant to the existence of a subsidy. One or the other is sufficient. If subsidies were deemed to exist only once a direct or potential direct transfer of funds had actually been effectuated, the Agreement would be rendered totally ineffective and even the typical WTO remedy (i.e. the cessation of the violation) would not be possible. We, therefore, consider that, the parties having agreed that PROEX payments are subsidies, the question of the form of financial contribution relates to the question of when the subsidy is paid, not when it comes into existence. This issue is taken up in section E.3. of these findings, where we consider whether Brazil has increased the level of its export subsidies.

7.14. For the foregoing reasons, we conclude that PROEX payments on exports of Brazilian regional aircraft are subsidies within the meaning of Article 1 of the SCM Agreement which are contingent upon export performance within the meaning of Article 3.1(a) of that Agreement.

D. ARE PROEX INTEREST RATE EQUALIZATION PAYMENTS "PERMITTED" BY ITEM (K) OF THE ILLUSTRATIVE LIST OF EXPORT SUBSIDIES?

7.15. We have found -- and Brazil does not dispute -- that PROEX payments are subsidies within the meaning of Article 1 of the SCM Agreement which are contingent upon export performance within the meaning of Article 3.1(a). Brazil does *not* concede, however, that these export subsidies are prohibited subsidies. Rather, Brazil contends that, although PROEX payments are export subsidies, they are nevertheless permitted by item (k) of the Illustrative List of Export Subsidies. Specifically, Brazil asserts that PROEX payments are the "payment by [governments] of all or part of the costs incurred by exporters or financial institutions in obtaining credits" within the meaning of item (k). Brazil further argues that,

¹⁹⁴ Brazil first submission, para. 6.1.

¹⁹⁵ The question asked by the Panel was: "Brazil stated in its first submission (para. 6.1) that it 'does not dispute the assertion that PROEX equalization payments for aircraft constitute an export subsidy.' Without prejudice to your material advantage defense under item (k) of the Illustrative List, do you acknowledge that PROEX payments otherwise fulfill the definition of a subsidy within the meaning of Article 1 which is contingent upon export performance within the meaning of Article 3.1(a)? If not, please identify precisely all elements of Articles 1 and 3 you consider are not satisfied and a detailed explanation of your views with regard to those elements."

pursuant to item (k), such payments are prohibited only "in so far as they are used to secure a material advantage in the field of export credit terms", and that *a contrario* "such payments are *permitted* in so far as they are *not* used to secure a material advantage in the field of export credit terms." Finally, Brazil argues that PROEX payments are not used to secure a material advantage in the field of export credit terms, because they are merely used to offset "Brazil risk" and Canada's subsidies to Bombardier. Accordingly, Brazil concludes that PROEX payments are permitted by the SCM Agreement.

7.16. Canada contests Brazil's arguments on a number of grounds. First, Canada disputes Brazil's view that the first paragraph of item (k) may be used to establish that a measure is "permitted" by the SCM Agreement. It is Canada's view – strongly supported by the European Communities as third party -- that footnote 5 to the SCM Agreement, which states that "[m]easures referred to in Annex I as not constituting export subsidies shall not be prohibited under this or any other provision of this Agreement", constitutes the only basis for arguing on the basis of the Illustrative List of Export Subsidies that a measure that does not fall within the scope of the Illustrative List is not prohibited, and Canada considers that the first paragraph of item (k) does not fall within the scope of that footnote. Second, Canada rejects Brazil's view that PROEX payments are the "payment by [governments] of all or part of the costs incurred by exporters or financial institutions in obtaining credits". Finally, Canada both disagrees with Brazil's interpretation of the "material advantage" clause in the first paragraph of item (k) and contends that PROEX payments are in fact "used to secure a material advantage" within the meaning of item (k).

7.17. In reviewing Brazil's item (k) defense, we note that in order for this Panel to rule in favour of Brazil we must find for Brazil on all of the following points. First, we must find that PROEX payments are the "payment by [governments] of all or part of the costs incurred by exporters or financial institutions in obtaining credits" within the meaning of item (k). Second, we must find that PROEX payments are not "used to secure a material advantage in the field of export credit terms" within the meaning of item (k). Finally, we must find that a "payment" within the meaning of item (k) which is not "used to secure a material advantage in the field of export credit terms" is "permitted" by the SCM Agreement even though it is a subsidy within the meaning of Article 1 of the SCM Agreement which is contingent upon export performance within the meaning of Article 3.1(a) of that Agreement. If we were to find against Brazil on any of these points, Brazil's item (k) defense would fail. Finally, we note Brazil's explicit acknowledgement that "its view of the 'material advantage' clause is that it constitutes an affirmative defense and, therefore, the burden of establishing entitlement to it is on the challenged party."¹⁹⁶

7.18. It is by no means clear to us that it is permissible to use the first paragraph of item (k) as the basis for an *a contrario* argument as asserted by Brazil,¹⁹⁷ or that PROEX payments in fact constitute the "payment by [governments] of all or part of the costs incurred by exporters or financial institutions in obtaining credits".¹⁹⁸ Even assuming for the sake of argument, however, that Brazil is correct with

¹⁹⁶ Brazil answer to panel question 41. See *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R, p. 16, adopted 23 May 1997 ("It is only reasonable that the burden of establishing [an affirmative] defence should rest on the party asserting it.").

¹⁹⁷ Footnote 5 to the SCM Agreement states that "[m]easures referred to in Annex I as not constituting export subsidies shall not be prohibited under [Article 3.1(a)] or any other provision of this Agreement." The only measures in the Illustrative List that are explicitly "referred to . . . as not constituting export subsidies" are export credit practices in conformity with the interest rate provisions of the Arrangement under the second paragraph of item (k). There are also a number of other cases, cited by Canada, where the Illustrative List affirmatively provides that a measure is not prohibited -- at least by that item -- or is permissible. The first paragraph of item (k), however, does not contain any such affirmative language, and would not appear to fall within the scope of footnote 5. Thus, a strong argument can be made that footnote 5 -- together with footnote 1 -- define the extent to which the Illustrative List can be used to establish that a measure is a "permitted" subsidy or, in the case of footnote 1, is not a subsidy at all. In light of our findings with respect to "material advantage", however, we need not decide this question.

¹⁹⁸ PROEX payments relating to export of Brazilian regional aircraft are provided in support of buyers' credits, i.e., export credits are extended to the foreign purchaser rather than to EMBRAER. Brazil's theory appears to be that lenders

respect to these two points, we consider Brazil's interpretation of the "material advantage" clause of item (k) is incorrect, and that, under a proper interpretation of that clause, Brazil has not demonstrated that PROEX interest rate equalization payments do not confer a material advantage in the field of export credit terms. As noted above, Brazil's "item (k)" defense can succeed only if Brazil prevails on all three legal issues. Because we dispose of Brazil's defense on the issue of whether PROEX interest rate equalization payments have been demonstrated not to confer a "material advantage", we need not decide whether Brazil's arguments on the first two issues are correct.

7.19. It will be recalled that, under item (k) of the Illustrative List, the following is an export subsidy:

"The grant by governments (or special institutions controlled by and/or acting under the authority of governments) of export credits at rates below those which they actually have to pay for the funds so employed . . . , or the payment by them of all or part of the costs incurred by exporters or financial institutions in obtaining credits, in so far as they are used to secure a material advantage in the field of export credit terms." (emphasis added).

Assuming for the sake of argument that PROEX payments are payments within the meaning of item (k), the question presented in this dispute is the benchmark that should be used in determining whether such payments are in fact "used to secure a material advantage." In Brazil's view, the proper benchmark for determining whether PROEX payments are "used to secure a material advantage in the field of export credit terms" is to compare the export credit terms of transactions supported by PROEX payments with the export credit terms available to purchasers of *Canadian* regional aircraft. As stated in the Finan Report, "Material advantage in the field of export credit terms cannot be measured by evaluating just one country's subsidy benefits. Rather, determining material advantage requires evaluating one country's set of export credit terms relative to another country's set by applying a consistent methodology appropriate under the facts and circumstances."¹⁹⁹

7.20. Brazil considers that, as a result of several factors, PROEX payments do not result in export credit terms for purchasers of *Brazilian* regional aircraft which secure a material advantage --i.e., are more favourable -- than the export credit terms available for purchasers of *Canadian* regional aircraft:

"The concept of material advantage, as noted above, includes comparison – advantage vis-à-vis someone or something. Two points of comparison are relevant to the determination in this dispute of whether PROEX is used by Brazil to secure a material advantage in the field of export credit terms: (1) Brazil risk and (2) Canada's subsidies to Bombardier. On either measure alone, PROEX provides no material advantage. When

providing export credits must borrow funds in order to finance their lending, that the export credits so funded are provided at below the lenders' cost of borrowing, and that PROEX payments are provided to compensate the lenders for this difference. In Brazil's view, this difference between the lender's cost of borrowing and the rate it charges for the export credits extended to purchasers therefore represents a "cost incurred by . . . financial institutions in obtaining credits." In addition, Brazil seeks to demonstrate that, although EMBRAER itself does not extend export credits to its customers, EMBRAER incurred certain costs in relation to the provision of buyer's credits to purchasers of Brazilian regional aircraft. Because our findings on the issue of "material advantage" dispose of Brazil's item (k) defense, we need not decide whether Brazil's view on this issue is correct. We note in passing, however, that -- assuming lenders providing export credits supported by PROEX payments are in fact providing export credits at below their cost of funds -- it is highly questionable whether that represents a cost for the lenders in "obtaining credits" as opposed to a cost incurred in *providing* credits.

¹⁹⁹ p. 1.9.

the two are considered together, it is clear that it is Canada's programmes, not Brazil's, that are used to secure a material advantage."²⁰⁰

7.21. Turning to the first "point of comparison" proposed by Brazil, Brazil argues that PROEX payments do no more than offset "Brazil risk". Specifically, Brazil contends that, due to the high level of risk perceived by international markets with respect to Brazilian borrowers, the cost to EMBRAER and to Brazilian financial institutions of raising funds to finance exports of Brazilian regional aircraft is higher than the cost to Bombardier and Canadian financial institutions of raising funds to finance exports of Canadian regional aircraft. Because PROEX payments merely offset in part that higher cost of funds, allowing export credit financing for Brazilian regional aircraft on terms that are closer to, but still less favourable than, those available for competing Canadian regional aircraft, those payments are not in Brazil's view used to secure a material advantage in the field of export credit terms.

7.22. With respect to the second "point of comparison", Brazil contends that "material advantage should be determined by comparison of the total subsidy packages" available to competing regional aircraft. In support of this view, Brazil argues that "the field of export credit terms" includes not only the interest rate and duration of the financing but also the price of the aircraft being financed. Brazil contends that Canada provides a wide range of "direct and indirect subsidies" for Canadian regional aircraft, and that these subsidies reduce the price of Canadian regional aircraft, the cost of credit to purchasers or other "export credit terms." Brazil concludes that, because PROEX payments do not fully offset these subsidies, those payments are not "used to secure a material advantage in the field of export credit terms".

7.23. As can be seen from the above arguments, Brazil's material advantage defense is based upon the principle that a consideration whether an item (k) payment "is used to secure a material advantage in the field of export credit terms" involves a comparison between the export credit terms of the transaction supported by the payment and the export credit terms of potential competing transactions. We do not agree. We note the definition of "advantage" in *Webster's New International Dictionary of the English Language*, cited by Brazil, as "a more favorable or improved position". Similarly, the *Shorter Oxford English Dictionary* defines "advantage" as "superior position". Thus, we concur with Brazil that the term "advantage" involves the concept of comparison. In our view, however, nothing in the text of the first paragraph of item (k) indicates that the examination of material advantage involves a comparison *with the export credit terms available with respect to competing products from other Members*. To the contrary, we consider that, in its ordinary meaning, a payment is "used to secure a material advantage in the field of export credit terms" where the payment is used to secure export credit terms that are materially more favorable than the terms that would have been available in the absence of the payment. Accordingly, we consider that an item (k) payment is "used to secure a material advantage" where the payment has resulted in the availability of export credit on terms which are more favourable than the terms that would otherwise be available in the marketplace to the purchaser with respect to the transaction in question.

7.24. Our understanding of the meaning of the "material advantage" clause is supported by its context in the SCM Agreement. Brazil's approach to determining whether an item (k) payment is used to secure a material advantage and thus represents an export subsidy differs strikingly from that applied elsewhere in the SCM Agreement with respect to determining whether a measure is a subsidy generally, or an export subsidy specifically. In this respect, the Agreement does not focus on the conditions under which a competing product from another Member is being sold and exported. Rather, the general approach of the SCM Agreement to determining whether a measure is a subsidy and thus subject to discipline is whether the measure confers a "benefit" within the meaning of Article 1. Although the concept of benefit is not defined in the SCM Agreement, its application in various circumstances suggests that one should examine

²⁰⁰ Brazil first submission, para. 6.6.

objective benchmarks, whether involving a comparison of the terms of the financial contribution to a market benchmark reflecting the terms under which the beneficiary of the financial contribution would be operating in the absence of the government financial contribution (as provided for in the calculation of the amount of the subsidy in terms of benefit to the recipient in a countervailing duty context under Article 14 of the Agreement)²⁰¹ or the existence of a cost to the government in providing the financial contribution (as envisioned by Annex IV relating to the calculation of the *ad valorem* subsidization for the purposes of the presumption of serious prejudice under Article 6.1(a) of the Agreement). In no case is it suggested that whether or not a benefit exists would depend upon a comparison with advantages available to a competing product from another Member.

7.25. Nor can we find any suggestion in either Article 3.1(a) of the SCM Agreement or the Illustrative List of Export Subsidies that whether a measure is a prohibited export subsidy should depend upon whether the measure merely offsets advantages bestowed on competing products from another Member. For example, item (c) of the Illustrative List treats as an export subsidy internal transport or freight charges on export shipments "on terms more favourable than for domestic shipments", irrespective of whether those charges are higher, lower or equal to the charges paid with respect to the shipments of competing products from other Members. Item (d) of the Illustrative List treats the provision of goods or services by a government for use in the production of exported goods as a prohibited export subsidy if the terms and conditions on which the goods or services are provided are more favourable than for the provision of goods for use in the production of goods for domestic consumption and if those terms and conditions are "more favourable than those commercially available on world markets *to their exporters*" (emphasis added). This last example is instructive, as the relevant test involves a comparison of the terms and conditions of the goods or services being provided by the government with the terms and conditions that would otherwise be available *to the exporters receiving the alleged export subsidy*; the fact that a foreign competitor had access to the same goods or services on better terms than those available to the exporters in question would not be a defense. In items (e), (f), (g), (h) and (i) of the Illustrative List, all of which relate to exemptions, remissions or deferrals of taxes or import charges, there is no hint that a tax advantage would not constitute an export subsidy simply because it reduced the exporter's tax burden to a level comparable to that of foreign competitors. In short, in asking us to look at the relative position of competitors in determining the disciplines applicable to item (k) payments, Brazil is asking us to construe that "material advantage" clause in a manner which does not conform to the general approach of the SCM Agreement.

7.26. In essence, Brazil's approach to "material advantage" boils down to an argument that an admitted export subsidy should not be deemed to be prohibited if it can be demonstrated merely to offset some advantage or advantages available to the competing product of another Member. We consider that such an interpretation would produce results that would be contrary to the object and purpose of the SCM Agreement. In our view, the object and purpose of the SCM Agreement is to impose multilateral disciplines on subsidies which distort international trade. It is for this reason that the SCM Agreement prohibits two categories of subsidies -- subsidies contingent upon exportation and upon the use of domestic over imported goods -- that are specifically designed to affect trade. The Brazilian approach to item (k), however, would effectively allow a Member to raise the provision of export subsidies --or indeed of any subsidy -- by the complaining Member as a defense justifying its own provision of export subsidies. This would entail a race to the bottom, as each WTO Member sought to justify the provision of

²⁰¹ The example of loans under Article 14 is instructive. Under Article 14(b), "a loan by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the loan pays on the government loan and the amount the firm would pay on a comparable commercial loan which the firm could actually obtain on the market." In other words, the relevant question is whether, as a result of the government intervention, the firm receiving the loan is better off than if that same firm had been required to obtain a loan in the marketplace.

export subsidies on the grounds that other Members were doing the same. Further, it should be recalled that under Articles 27 and 29 of the SCM Agreement certain Members are entitled to special and differential treatment and are not subject to the prohibition on export subsidies. It may be queried whether, if we were to interpret item (k) in the manner suggested by Brazil, developed country Members would in effect be authorized to match the export credit terms, however favourable, offered by developing country Members without falling afoul of the SCM Agreement's prohibition on the provision of export subsidies, with its consequent weakening of the SCM Agreement's disciplines on export subsidies. Such results certainly would not be consistent with the object and purpose of the Agreement identified above.

7.27. Finally, Brazil's interpretation of the material advantage clause would in our view generate results that are manifestly unreasonable in the context of the SCM Agreement. First, under Brazil's interpretation the determination whether an item (k) payment represented an export subsidy would require in each case an examination of the terms and conditions of the export credits available for competing products of another Member. Thus, a Member seeking to determine whether it could provide item (k) payments without violating Article 3 of the SCM Agreement would be required to first assess the terms and conditions under which export credits were available with respect to the competing products of all other Members. This might well prove impossible, given that the terms and conditions of a given export credit transaction are confidential business information not generally available to the public at large. Second, a payment could be found to be a prohibited export subsidy when challenged by one complainant yet found not to be a prohibited export subsidy when challenged by a different complainant whose exporters had access to export credit on more favourable terms, thus generating inconsistent results under the WTO dispute settlement system. Third, export subsidies that were "permitted" at a given moment might be transformed into prohibited export subsidies as a result of changes in the terms and conditions under which export credits were available in other Members.²⁰² We consider that an interpretation of item (k) that would make the status of a Member's measures as a possible export subsidy dependent on factors outside its knowledge and control, and that could generate such unpredictable results, is unreasonable and thus to be avoided.

7.28. Even if we were to agree with Brazil – which we do not -- that in order to ascertain whether an item (k) payment secures a material advantage it is necessary to examine the export credit terms available with respect to competing products exported from other Members, we still could not agree with Brazil's interpretation of the clause "in the field of export credit terms". It will be recalled that Brazil's interpretation of that clause would include as an export credit term the price at which a product was sold, and would therefore allow Brazil to offset through item (k) payments all subsidies provided to Bombardier that could reduce the price at which regional aircraft exported by that manufacturer could be sold and thus reduce the amount of the transaction to be financed. In our view, this interpretation stretches far beyond the ordinary meaning of the phrase in question. In its ordinary meaning, the field of export credit terms would refer to items directly related to export credits, such as interest rates, grace periods, transaction costs, maturities and the like. We consider that this interpretation is supported contextually by item (k) itself, which refers to a loan's "maturity and other credit terms". We see nothing in the ordinary meaning of the phrase to suggest that "the field of export credit terms" generally encompasses the price at which a product is sold.²⁰³

²⁰² In response to a question from the Panel, Brazil acknowledges this, stating that "[i]t is true that under Brazil's theory, a permitted subsidy could become prohibited and vice versa depending on the action of other Members, but, Brazil submits, this is a logical consequence of the ordinary meaning of the language of item (k)."

²⁰³ We recognize that there might be cases where an item (k) payment, rather than being used to reduce the interest rate or improve some other term related to the transaction, is applied to reduce the amount of the transaction financed. In fact, evidence on the record suggests that PROEX payments are sometimes used in precisely this manner, in that the financial institution providing the export credits, rather than using the PROEX payments to reduce the interest rate charged to the purchaser of an EMBRAER regional aircraft, may also sell the NTN-1 bonds it receives from the Government of Brazil in the

7.29. Brazil's arguments regarding the meaning of the "material advantage" clause seek to characterize its interpretation of that clause as necessary to protect the rights of developing country Members. Brazil's argument, if we understand it correctly, is that developed country Members have negotiated for themselves, in the second paragraph of item (k), a special safe haven from the export subsidy prohibition for export credit practices that conform to the interest rate provisions of the OECD Arrangement on Guidelines for Officially Supported Export Credits ("the OECD Arrangement"). Because of their high sovereign risk premiums, however, most developing country Members cannot afford to borrow on international capital markets at high rates of interest in order to engage in direct financing on terms consistent with the Arrangement. Under the first paragraph of item (k), however, developing country Members may – if Brazil's interpretation of "material advantage" is accepted – effect a reduction in the interest rates charged by financial institutions on export credits for their exports by making item (k) payments, at a lower cost than were the developing country Member to provide export credits directly at the same interest rates. Accordingly, and in Brazil's words, developing country Members "bargained . . . for the 'material advantage' language of item (k) precisely because, when Article 27's protection expires, they needed something they could afford in view of the fact that developed countries had their own self-designed exemption, which is presently in the second paragraph of item (k)."

7.30. We find Brazil's effort to characterize the interpretation of the first paragraph of item (k) as a developed/developing country issue unconvincing. First, we note that the "material advantage" clause has its origins in the Tokyo Round Subsidies Code²⁰⁴ and was carried over unchanged into the SCM Agreement. Given that developing country signatories of the Code were exempted by Article 14.2 of the Code from the commitment not to grant export subsidies on products other than certain primary products, it seems unlikely that the material advantage clause was conceived at that time as a protection for developing countries. Nor has Brazil submitted any substantial support for the proposition that developing country Members sought to retain the "material advantage" clause during the Uruguay Round in order to retain the ability to offset the high sovereign risk of developing country Members through item (k) payments.²⁰⁵

7.31. Second, we believe that Brazil is incorrect in its underlying assumption that the second paragraph of item (k) provides a safe haven only with respect to direct export credit financing. The second paragraph of item (k) provides that "an export credit practice", whether of an Arrangement Participant or of a non-Arrangement WTO Member, which is in conformity with the "interest rate provisions" of the OECD Arrangement shall not be considered an export subsidy prohibited by the SCM Agreement. Chapter I:2 of the OECD Arrangement, titled "Scope of Application", provides that the Arrangement

market and use the proceeds to provide a cash discount to the purchaser. We do not preclude that, in such a particular situation, the field of export credit terms might be deemed to include the price of the goods being financed. This is a far cry, however, from the broad argument made by Brazil.

²⁰⁴ Agreement on Interpretation and Application of Articles VI, XVI and XXIII of the General Agreement on Tariffs and Trade.

²⁰⁵ In response to a question from the Panel, Brazil argues that a proposal during the Uruguay Round by "a developed country" to modify the first paragraph of item (k) by, *inter alia*, deleting the material advantage clause was rejected by Brazil and other developing countries. The informal negotiating document submitted by Brazil in relation to this answer tells us little about the issues before this Panel, however. First, the document in question says nothing about which countries made and which countries rejected the proposal. More importantly, the proposal not only would have deleted the "material advantage" clause, but would also have changed the benchmark for when direct export financing constitutes an export subsidy from a cost of borrowing standard to a market benchmark ("terms and conditions more favourable than the terms and conditions the borrower would otherwise obtain for financing comparable transactions"). An accompanying note focuses on the latter issue, and provides no explanation as to why the proposed deletion of the "material advantage" clause was rejected.

"shall apply to all official support for exports of goods and/or services . . . which have repayment terms of . . . two years or more . . . regardless of whether the official support is given by means of direct credit/financing, refinancing, *interest rate support*, guarantee or insurance" (emphasis added).

Accordingly, a developing country Member could under the second paragraph of item (k) provide interest rate support to reduce the interest rates on export credits to the levels allowed by the OECD Arrangement if it considered that direct financing at those rates was too expensive.²⁰⁶ Thus, Brazil's view that developing country Members cannot afford to use the safe haven of the second paragraph of item (k) and must therefore rely on the "material advantage" clause of the first paragraph of item (k), as interpreted by Brazil, is also incorrect.

7.32. Finally, not only is item (k) on its face *not* a provision relating to special and differential treatment – which provisions may be found in Article 27 of the SCM Agreement – but Brazil's interpretation of material advantage could actually undermine the value of Article 27 for developing country Members. In particular, if the Panel were to accept the interpretation of material advantage advanced by Brazil, the first paragraph of item (k) could – as noted in paragraph 7.26 above -- be used by developed country Members as a justification to match, with export subsidies that would otherwise be prohibited, export subsidies provided by developing countries consistent with Article 27. Thus, while Brazil's interpretation of "material advantage" may serve the interests of one particular developing country Member with respect to its defense of one particular type of subsidy in one particular dispute, it cannot be generalized from this that Brazil's interpretation of the "material advantage" clause is necessary to protect the interests of developing country Members collectively. Rather, Brazil's interpretation would serve to benefit developing country Members only to the extent that one considers that a general lowering of the level of SCM Agreement disciplines on export subsidies applicable to all WTO Members is in the interests of developing country Members.

7.33. For the reasons discussed above, we consider that an item (k) payment is "used to secure a material advantage" and is thus a prohibited export subsidy where the payment has resulted in the availability of export credit on terms which are more favourable than the terms that would otherwise be available in the marketplace to the purchaser with respect to the transaction in question.

7.34. Applying the above standard to the case at hand, we consider it evident that PROEX payments result in the availability of export credit for Brazilian regional aircraft on terms which are more favourable than the terms that would otherwise be available with respect to the transaction in question. This follows from the very design of PROEX and the manner in which PROEX interest rate equalization operates. As characterized by Brazil, the purpose of PROEX payments is to improve the terms of export credit financing that would otherwise be available to purchasers of Brazilian regional aircraft and other

²⁰⁶ Because Brazil has not invoked the second paragraph of item (k) as a defense in this dispute, we need not consider the application of that provision to PROEX payments. However, we note that the *Finan Report's* contention that PROEX interest rate equalization would not "by definition" be permitted by the OECD Arrangement because it is "designed to offset a portion of Brazil risk" is mistaken. In support of its contention, the *Finan Report* relies on paragraph 20 of the OECD Arrangement, which provides that:

"[t]he Participants providing official support through direct credits/financing, refinancing, export credit insurance and guarantees, shall charge no less than the minimum premium benchmarks for the sovereign risk and the country credit risk, irrespective of whether the buyer/borrower is a private or a public entity."

Paragraph 20, however, excludes "interest rate support" from the categories of official support for which a minimum premium must be charged, presumably because in the case of interest rate support the government does not bear the risk of loss in the case of default. In any event, these premia relate to the risk relating to the country of the *buyer/borrower*, not that of the *lender*.

Brazilian products by offsetting "Brazil risk". Thus, under the PROEX interest rate equalization scheme EMBRAER and its export customers are free to negotiate the best export credit terms they may obtain in the market, irrespective of whether the lender is a Brazilian or foreign financial institution. As a tool to obtain the most favourable terms possible, they may request a letter of commitment from the Government of Brazil committing Brazil to provide fixed PROEX interest rate equalization payments of 3.8 percentage points to the lender; there is no requirement to demonstrate in a particular case that a 3.8 percentage point level is necessary to compensate for the lender's higher cost of funds. The payments may be used to improve the export credit terms in one of several ways. For example, the availability of the payments may be used to negotiate lower interest rates for the export credits in question than would otherwise be available for the transaction. In the alternative, the lending bank may agree to discount the bonds and to pass the sum along to the purchaser/borrower as a cash discount. In any event, we consider that, as a matter of logic, the payments will as a natural consequence allow EMBRAER and the purchaser to negotiate more favourable export credit terms than they could otherwise achieve in the marketplace.

7.35. We recall Brazil's acknowledgement that its "material advantage" argument constitutes an affirmative defense and, therefore, the burden of establishing entitlement to it is on Brazil. In this case, not only has Brazil failed to demonstrate that PROEX payments do not allow the purchaser of Brazilian regional aircraft to obtain more favourable export credit terms than the terms that would otherwise be available to the purchaser with respect to the transaction in the market, but Brazil has conceded to the contrary. Thus, in response to a question from the Panel²⁰⁷, Brazil stated that:

"PROEX presumably would always be more favorable to the purchaser than the terms it could obtain on its own; otherwise, the purchaser would have no interest in PROEX. If the PROEX-supported export credit term is compared merely to the credit terms a particular buyer could obtain on its own, PROEX could never provide assistance and always would be at a disadvantage vis-à-vis competitors supported by an export credit agency, whether that agency's programmes were or were not consistent with WTO obligations."

Brazil makes a similar admission in the *Finan Report*, where it states that:

"Brazil's PROEX programme, applied to support exports of regional aircraft, acts to reduce the cost of export financing for the aircraft buyer."²⁰⁸

Thus, we consider that as a factual matter Brazil does not argue that PROEX payments do not confer a "material advantage" as that term has been interpreted by this Panel.

7.36. Neither has Brazil asserted, much less submitted evidence supporting an assertion, that any specific transactions relating to the export of Brazilian regional aircraft supported by PROEX payments have not resulted in export credit terms that are more favourable than the terms that would otherwise have

²⁰⁷ The question asked by the Panel was as follows: "Canada argues that the phrase 'in the field of export credit terms' as used in item (k) of Annex I of the SCM Agreement is limited to the interest rates and other transaction costs. Assuming for the sake of argument that this view is correct, what would be the appropriate benchmark for a comparison? Specifically, should the export credit terms of the transaction supported by PROEX interest rate equalization be compared to the export credit terms that would be available to the purchaser of EMBRAER aircraft on the market for the purchase of those aircraft if the PROEX interest rate equalization were not available for the transaction, or should it relate to the export credit terms available (including through official financing at OECD consensus rates by a Participant to the OECD Arrangement) to the purchaser if it purchased a competing civil aircraft?" Brazil responded that, "[w]ith regard to the two specific examples, Brazil would answer 'The latter'". The quote above followed.

²⁰⁸ *Finan Report*, p. 1.2.

been available to the purchaser in the market with respect to those transactions. In fact, Brazil has not submitted any significant evidence regarding the specific terms and conditions, such as the interest rate, at which export credits supported by PROEX payments were provided, much less information regarding the export credit terms that would otherwise have been available with respect to the transaction in the market. Brazil did assert that, "in transactions when the lender was inside Brazil, the actual interest rate was always above LIBOR or the OECD rate in practice." But even with respect to this assertion, which in any event is not relevant in our view to the proper application of the "material advantage" clause, Brazil has not provided any supporting evidence. To the contrary, in response to a question from the Panel asking for specific information with respect to each transaction alleged by Brazil to be at or above the CIRR rate²⁰⁹, Brazil responded that:

"[t]his information requested by the Panel is not readily available to PROEX administrators. These authorities simply ensure that the bonds are issued to the agent bank and have no control, jurisdiction or access to specific details of the commercial transactions" ²¹⁰

In fact, with the respect to the one transaction supported by PROEX payments with respect to which Brazil has provided detailed information -- on a Business Confidential basis -- it is clear that the PROEX payments resulted in a very substantial improvement in the export credit terms as compared to the terms that could have been obtained in the absence of the payments.

7.37. In conclusion, we consider that an item (k) payment is "used to secure a material advantage" where the payment has resulted in the availability of export credit on terms which are more favourable than the terms that would otherwise have been available to the purchaser with respect to the transaction in question. Even if we were to assume, as argued by Brazil, that PROEX payments are the "payment by [a government] of all or part of the costs incurred by exporters or financial institutions in obtaining credits", and that such payments can be deemed to be "permitted" by item (k) where they are not "used to secure a material advantage in the field of export credit terms" -- issues we need not here decide -- Brazil has failed to demonstrate the PROEX payments are not "used to secure a material advantage in the field of export credit terms". Accordingly, we reject Brazil's affirmative defense based on item (k) of the Illustrative List.

E. IS THE PROHIBITION ON EXPORT SUBSIDIES INAPPLICABLE TO BRAZIL BY REASON OF ITS STATUS AS A DEVELOPING COUNTRY MEMBER?

7.38. In the foregoing sections of this Report, we have found that PROEX payments are subsidies within the meaning of Article 1 of the SCM Agreement, and that those subsidies are contingent upon exportation within the meaning of Article 3.1(a) of that Agreement. Further, we have found that Brazil has not demonstrated that those subsidies are "permitted" by the first paragraph of item (k) of the SCM Agreement. In the usual case, this would be sufficient to establish that the subsidies in question are

²⁰⁹ The CIRR rate is the "commercial interest reference rate" which represents the minimum interest rate to be charged on officially supported export credits under the OECD Arrangement.

²¹⁰ The question posed by the Panel was: For each sale of EMBRAER regional aircraft supported by PROEX interest rate equalization which you contend was at an interest rate at or above the CIRR rate (taking into account the interest rate equalization), please specify: (a) the purchaser; (b) the financial institution providing the financing; (c) the date of the transaction; the currency in which export financing was provided; (e) the maturity of the financing; (f) the terms of the financing, including whether the interest rate is fixed or variable and, in the latter case, how it is established; (g) the rate of interest before and after PROEX interest rate equalization is considered. Please provide any supporting documentation which you consider necessary to support your factual assertions in this regard."

prohibited by Article 3 of the SCM Agreement. In this case, however, the parties agree that Brazil is a developing country Member within the meaning of the SCM Agreement. As such, Brazil is entitled to the extensive special and differential treatment accorded to such Members by Article 27 of the SCM Agreement. Accordingly, and as required by Article 12.11 of the DSU, we must now consider whether, under the facts of this case, Brazil is shielded from the Article 3.1(a) prohibition by reason of Article 27.

1. Is Article 27 *Lex Specialis* to Article 3?

7.39. Brazil argues *en passant* that Article 27 is *lex specialis* to Article 3, in that it provides special rules with regard to export subsidy programmes of developing country Members. In other words, it is Brazil's view that the specific provisions of Article 27 relating to developing country Members' export subsidies displace the general provisions of Article 3.1(a), and that it is therefore not possible for developing country Members to act in a manner inconsistent with Article 3. Because Canada has not alleged that Brazil has violated Article 27 of the SCM Agreement, nor is any such claim within the Panel's terms of reference, Brazil considers that the Panel must deny Canada's complaint in this dispute.

7.40. Brazil has not vigorously pursued its *lex specialis* argument, and for good reason. In our view, Brazil's argument cannot be reconciled with the ordinary meaning of Article 27.2 of the SCM Agreement. It will be recalled that Article 27.2 provides that "[t]he prohibition of paragraph 1(a) of Article 3 shall not apply to . . . developing country Members [other than those referred to in Annex VII] for a period of eight years from the date of entry into force of the WTO Agreement, *subject to compliance with the provisions of paragraph 4 [of Article 27]*" (emphasis added). It is evident to us from this language that Article 27 does not "displace" Article 3.1(a) of the SCM Agreement unconditionally as argued by Brazil. Rather, the prohibition of Article 3.1(a) shall not apply "subject to compliance with the provisions of paragraph 4". The exemption for developing country Members other than those referred to in Annex VII from the application of the Article 3.1(a) prohibition on export subsidies is clearly conditional on compliance with the provisions in paragraph 4 of Article 27. Thus, we consider that, where the provisions in Article 27.4 have not been complied with, the Article 3.1(a) prohibition applies to such developing country Members.

7.41. Although we have addressed Brazil's *lex specialis* argument for the sake of completeness, Brazil arguably abandoned its *lex specialis* argument during the course of the proceedings. Thus, in a question to Brazil the Panel quoted Article 27.2(b) and stated that "[i]t could be argued that, by negative implication, the prohibition does apply. Please comment." Brazil responded that "[t]his is true, but the central question is which party bears the burden of proof . . ." Accordingly, it is to that question that we now turn.

2. Article 27.4 conditions and burden of proof

7.42. As explained above, we consider that the prohibition on export subsidies applies to developing country Members other than those referred to in Annex VII²¹¹ in the event of non-compliance with the provisions in Article 27.4. In Canada's view, Article 27.4 contains three relevant conditions. *First*, export subsidies must be phased out within the eight-year period. *Second*, the level of export subsidies must not increase during that period. *Third*, export subsidies must be eliminated within a period shorter than eight years when the use of these subsidies is not consistent with the Member's development needs.

²¹¹ For the sake of convenience, we will generally refer to "developing country Members other than those referred to in Annex VII" simply as "developing country Members." This should not be construed as suggesting that the non-application of Article 3.1(a) to developing country Members referred to in Annex VII is conditioned on compliance with the provisions of Article 27.4.

Before turning to a discussion of the specific elements of Article 27.4, however, we must consider the issue, which has been argued extensively by the parties, regarding who bears the burden of proof with respect to compliance with the provisions of Article 27.4.

7.43. Article 27.2(b) of the SCM Agreement provides:

27.2 The prohibition of paragraph 1(a) of Article 3 shall not apply to:

.....

(b) developing country Members for a period of eight years from the date of entry into force of the WTO Agreement, subject to compliance with the provisions of paragraph 4.

Article 27.4 of the SCM Agreement reads, in relevant part:

27.4 Any developing country Member referred to in paragraph 2(b) shall phase out its export subsidies within the eight-year period, preferably in a progressive manner. However, a developing country Member shall not increase the level of its export subsidies⁵⁵ and shall eliminate them within a period shorter than that provided for in this paragraph when the use of such export subsidies is inconsistent with its development needs....

⁵⁵For a developing country Member not granting export subsidies as of the date of entry into force of the WTO Agreement, this paragraph shall apply on the basis of the level of export subsidies granted in 1986.

7.44. The parties are in fundamental disagreement about the legal nature of the relationship between Article 3.1(a) and the above-cited provisions of Article 27. In particular, they disagree as to whether the provisions in Article 27.4 are an integral part of Canada's claim of violation of Article 3.1(a) with respect to which Canada bears the burden of proof, or whether these provisions constitute an "exception" from, or "affirmative defense" to, the prohibition laid out in Article 3.1(a) with respect to which Brazil bears the burden of proof. Canada contends that, because Article 27 reflects special and differential treatment for developing country Members, it is an exception to the general obligations of the SCM Agreement. In Canada's view, Article 27.2(b) sets forth a "limited and conditional exception" to the prohibition in Article 3.1(a). Canada relies on the Panel Report in *Argentina – Footwear I*²¹² for the proposition that "it is for the party invoking an exception or an affirmative defense to prove that the conditions contained therein are met". According to Canada, in order to benefit from the "exception" in Article 27.2(b), Brazil bears the burden of demonstrating that it has complied with the conditions of Article 27.4.

7.45. Brazil disputes that Article 27.2(b) can be characterized as an "exception" to the prohibition set out in Article 3.1(a), or that it bears the burden of proof with respect to compliance with that provision and with the conditions stipulated in Article 27.4. For Brazil, Article 27 consists of carefully negotiated language that reflects a carefully drawn balance of rights and obligations. Brazil points out that the text of the provision states "clearly and unequivocally" that "the prohibition of paragraph 1(a) of Article 3 shall not apply" to developing countries, subject to the conditions in Article 27.4. In Brazil's view,

²¹² *Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items*, WT/DS56/R, para. 6.35, adopted 22 April 1998.

Canada, as the complaining party, bears the burden of establishing that Brazil has not complied with these conditions. The third parties, the European Community and the United States, support Canada's position.

7.46. There appears to be no overriding general principle to guide a panel in distinguishing between an element of a claim of violation of a provision of the WTO Agreement and an "exception" from, or "affirmative defence" to, a provision of the WTO Agreement. However, it is clear that the mere characterization of a provision as an "exception" will not necessarily determine which party bears the burden of proof with respect to establishing the elements contained in that provision. Thus, we note that, in *EC Measures Concerning Meat and Meat Products (Hormones)*, for example, the Appellate Body stated that:

"The general rule in a dispute settlement proceeding requiring a complaining party to establish a *prima facie* case of inconsistency ... is *not* avoided by simply describing that provision as an 'exception.'"²¹³

7.47. Nevertheless, it is well-established in WTO practice that a party who asserts the affirmative of a particular claim or defence bears the burden of proof with respect to that claim or defense. As the Appellate Body stated in *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India*:

"... it is a generally-accepted canon of evidence in civil law, common law, and in fact, most jurisdictions, that the burden of proof rests upon the party, whether complaining or defending, who asserts the affirmative of a particular claim or defence. If that party adduces evidence sufficient to raise a presumption that what is claimed is true, the burden then shifts to the other party, who will fail unless it adduces sufficient evidence to rebut the presumption."²¹⁴

7.48. Therefore, in determining which party bears the burden of proof in this case with respect to the compliance with the provisions of Article 27.4 of the SCM Agreement, it is necessary to consider whether that provision is in the nature of an element of a claim of violation of Article 3.1(a) where the Member complained against is a developing country Member within the meaning of Article 27.2(b), or whether it is in the nature of an affirmative defence that may be invoked by such a developing country Member in response to a claim of inconsistency with Article 3.1(a). If it is an element of a claim of inconsistency with Article 3.1(a), then, in this case, it would fall to Canada, as the complaining party, to adduce evidence sufficient to raise a presumption that Brazil was *not in compliance* with the conditions set out in Article 27.4, at which point the burden would shift to Brazil to rebut this presumption. If, on the other hand, Article 27.4 is in the nature of an affirmative defence, it would be for Brazil to adduce evidence sufficient to raise a presumption that it was *in compliance* with the provisions in Article 27.4, at which point the burden would shift to Canada to rebut this presumption.

7.49. In our view, a determination of the nature of this provision, and an examination of which party bears the burden of proof under it, must turn on the actual wording of the relevant text of the Agreement in its context, and in light of the object and purpose of the SCM Agreement. We note that Article 27.2(b)

²¹³ WT/DS26/AB/R, WT/DS48/AB/R, para. 104, adopted 13 February 1998.

²¹⁴ WT/DS33/AB/R, p. 14, adopted 23 May 1997.

contains an explicit textual link between itself and Article 27.4, as well as between Article 3.1(a) and Article 27.4. It states:

"The prohibition of paragraph 1(a) of Article 3 shall not apply to: ... other developing country Members for a period of eight years from the date of entry into force of the WTO Agreement, *subject to compliance with the provisions in paragraph 4.*" (emphasis added)

Because of this explicit textual linkage between Article 27.2(b) and Article 27.4, we consider that these paragraphs must be read in conjunction in order to determine the legal nature of the conditions contained in Article 27.4. Due to the wording of Article 27.2(b) highlighted above, we believe this provision to be determinative for the issue of allocating the burden of proof with respect to the conditions contained in Article 27.4.

7.50. An essential element in establishing a claim of inconsistency with a provision of the WTO Agreement is to demonstrate that the particular provision *applies* to the particular Member in question and to the particular factual situation in a given dispute. Part and parcel of asserting the affirmative of a particular claim is to demonstrate that the legal provision forming the basis for that claim applies to the Member against whom that legal provision is being invoked. Naturally, there will be no inconsistency with a given provision if a Member is explicitly excluded from its scope of application or a situation is explicitly identified in the text of the Agreement as falling outside the scope of application of a particular provision. In this regard, we recall that Article 27.2(b) states that: "The prohibition of paragraph 1(a) of Article 3 *shall not apply to*: ... other developing country Members for a period of eight years from the date of entry into force of the WTO Agreement, subject to compliance with the provisions in paragraph 4." (emphasis added) Clearly, on the basis of the plain meaning of the text of the provision, developing country Members falling within Article 27.2(b) -- that is, developing country Members (other than those referred to in Annex VII) that are in compliance with the provisions of Article 27.4 -- do not fall within the scope of application of the prohibition contained in Article 3.1(a) until 1 January 2003.

7.51. We consider that this interpretation is supported by the context of Article 27.2(b). Article 27 is entitled "Special and Differential Treatment of Developing Country Members" and this provision constitutes Part VIII of the SCM Agreement, entitled "Developing Country Members". Thus, the context of the provisions indicates that they extend "special and differential treatment" to developing country Members.

7.52. The context of Article 27.2(b) also includes Article 27.3 and Article 27.7 of the SCM Agreement. Article 27.7 reads:

27.7 The provisions of Article 4 shall not apply to a developing country Member in the case of export subsidies which are in conformity with the provisions of paragraphs 2 through 5. The relevant provisions in such a case shall be those of Article 7.

We consider that, analogous to Article 27.2(b) in relation to Article 3.1(a), this provision would exclude developing country Members from the scope of application of Article 4 in certain circumstances. The phrase "subject to compliance with the provisions in paragraph 4" contained in Article 27.2(b) can, in our view, be seen as analogous to the phrase "which are in conformity with paragraphs 2 through 5" contained in Article 27.7. This supports an interpretation of Article 27.2(b) that developing country Members are excluded from the scope of application of the substantive obligation in question provided that they comply with certain specified conditions.

7.53. Moreover, Article 27.3 states:

27.3 The prohibition of paragraph 1(b) of Article 3 shall not apply to developing country Members for a period of five years, and shall not apply to least-developed country Members for a period of eight years, from the date of entry into force of the WTO Agreement.

This provision reflects that developing country Members are excluded outright from the scope of application of the substantive obligation of Article 3.1(b) (the prohibition on subsidies contingent on the use of domestic over imported goods) for a stipulated period of time. As contextual for Article 27.2(b), it supports the view that the relevant provisions of Article 27, which extend "special and differential treatment to developing countries", serve to exclude, in a qualified or unqualified manner, certain developing countries from the scope of application of certain substantive obligations found elsewhere in the Agreement for specified periods of time. Moreover, in Article 27.1, Members "recognize that subsidies may play an important role in economic development programmes of developing country Members". Therefore, on the basis of the text and context of Article 27.2(b), we consider that Article 27.2(b) serves to exclude the developing country Members referred to in that provision from the scope of application of the prohibition in Article 3.1(a), subject to compliance by the developing country Member in question with the provisions in Article 27.4.

7.54. This view, derived from the text and context of Article 27.2(b), reflects a legal relationship between Article 3.1(a), Article 27.2(b) and 27.4 of the SCM Agreement that is qualitatively different from the relationship between, for instance, the substantive obligations contained in Articles I or III of the GATT 1994 and the affirmative defences set out in the "general exceptions" of Article XX of the GATT 1994. Article 27.2(b) excludes from the scope of application of Article 3.1(a) a developing country Member referred to in Article 27.2(b) for a period of eight years from the date of entry into force of the WTO Agreement. In other words, Article 27.2(b) recognizes the autonomous right of certain developing country Members to grant or maintain export subsidies during a stipulated period. According to the specific language of that provision, this right is "subject to compliance with the provisions of paragraph 4" of Article 27. Paragraph 4 of Article 27 then sets out the conditions with which a qualifying developing country Member must comply in order to be excluded from the scope of application of the prohibition in Article 3.1(a), that is, in order that the substantive obligation in Article 3.1(a) not apply to it. This contrasts markedly with a situation that could arise with respect to the affirmative defences set out in Article XI:2 or XX of the GATT 1994, where there is no dispute that the substantive obligation contained in, say, Article I or III of the GATT 1994, applies to the Member in question, but that Member argues that, while it may have acted inconsistently with a particular provision, it should be excused from the substantive obligation contained in that provision.²¹⁵

²¹⁵We note that the Appellate Body stated the following in *EC – Hormones* (para. 104), in relation to the relationship between Article 3.1 and Article 3.3 of the *SPS Agreement*:

"[t]he Panel posits the existence of a "general rule – exception" relationship between Article 3.1 (the general obligation) and Article 3.3 (an exception) and applies to the *SPS Agreement* what it calls "established practice under GATT 1947 and GATT 1994" to the effect that the burden of justifying a measure under Article XX of the GATT 1994 rests on the defending party. It appears to us that the Panel has misconceived the relationship between Articles 3.1, 3.2 and 3.3, a relationship discussed below, which is qualitatively different from the relationship between, for instance, Articles I or III and Article XX of the GATT 1994. Article 3.1 of the *SPS Agreement* simply excludes from its scope of

7.55. We draw, from WTO practice, further support for our view that the nature of the legal relationship between Articles 3.1, 27.2(b) and 27.4 of the SCM Agreement differs qualitatively from that between, say, Article III and Article XX of the GATT 1994. We note that, in addressing the nature of Article 6 of the Agreement on Textiles and Clothing in *United States – Shirts and Blouses*, the Appellate Body stated that Articles XI and XX are "limited exceptions from obligations under certain other provisions of GATT 1994, *not positive rules establishing obligations in themselves*". (emphasis added) Although Article 27.2(b) does not, in itself, establish any obligations, Article 27.4 does impose certain obligations, i.e., the obligation on developing country Members within the meaning of Article 27.2(b) to "phase out its export subsidies within the eight-year period, preferably in a progressive manner"; to "not increase the level of its export subsidies" and "to eliminate them within a period shorter than [eight years]when the use of such export subsidies is inconsistent with its development needs". This is not to say that Article 27.4 would necessarily form the legal basis for a separate claim of violation of the SCM Agreement.²¹⁶ Rather, because of the explicit textual link found in Article 27.2(b) between Articles 3.1(a), 27.2(b) and 27.4, the requirements of Article 27.4 must be considered in conjunction with Article 3.1(a) of the SCM Agreement in order to establish a claim of violation of that provision against a Member that is a developing country Member within the meaning of Article 27.2(b).

7.56. The fundamental issue before us, therefore, is whether the prohibition in Article 3.1(a) of the SCM Agreement *applies* to the developing country Member in question, rather than whether the developing country Member, having been found to be subject to the substantive obligations of Article 3.1(a), and having been found to have acted inconsistently with these obligations, can find justifying protection by invoking Article 27.2(b) in conjunction with Article 27.4. In our view, until non-compliance with the conditions set out in Article 27.4 is demonstrated, there is also, on the part of a developing country Member within the meaning of Article 27.2(b), no inconsistency with Article 3.1(a). We recall the words of the Appellate Body in *United States – Shirts and Blouses* that "a party claiming a violation of a provision of the WTO Agreement by another Member must assert and prove its claim."²¹⁷ Applying this terminology to the case at hand, we consider that, in order to assert and prove a claim of violation of Article 3.1(a) with respect to a Member that is a developing country Member within the meaning of Article 27.2(b), the Member asserting the claim must demonstrate that the substantive obligations contained in Article 3.1(a) of the SCM Agreement apply to the Member in question. In order to do this, the Member asserting the claim must demonstrate that the developing country Member concerned has not complied with the conditions stipulated in Article 27.4.

7.57. Where, as here, it is agreed that the Member in question is a developing country Member within the meaning of Article 27.2(b), it is for the Member alleging a violation of Article 3.1(a) of the SCM Agreement to demonstrate that the substantive obligation in that provision -- the prohibition on export subsidies -- applies to the developing country Member complained against. That is, it is for the complaining Member to demonstrate that the developing country Member in question is not in compliance with at least one of the elements laid out in Article 27.4. In light of the above, we consider that, in order to determine whether Brazil has acted inconsistently with Article 3.1(a), it is for Canada to establish that Article 3.1(a), in fact, applies to Brazil at the present time. Accordingly, we find that Canada bears the burden of proving that Brazil is not in compliance with the provisions of Article 27.4.

application the kinds of situations covered by Article 3.3 of that Agreement" (footnotes omitted).

²¹⁶ Given that Canada has made no claim of a violation of Article 27.4, this is an issue we need not and do not decide in this dispute.

²¹⁷ WT/DS33/AB/R, p. 16, adopted 23 May 1997.

3. Has Brazil increased the level of its export subsidies?

7.58. Having resolved the question of burden of proof, we now turn to the first element of Article 27.4 identified by Canada, whether Brazil has increased the level of its export subsidies. It will be recalled that Article 27.4 provides, in relevant part, that "a developing country Member shall not increase the level of its export subsidies⁵⁵ . . .". Canada asserts that Brazil has increased the level of its export subsidies. Brazil asserts, on the basis of the same data, that it has not increased the level of its export subsidies. Accordingly, before turning to the undisputed factual information submitted by the parties, we must consider a number of legal issues relating to the proper interpretation of this provision.

7.59. The first issue presented is whether "the level of export subsidies" referred to in Article 27.4 means the overall level of export subsidies of a Member during a given period, the level of export subsidies with respect to some given product during that period, or some other measurement. With respect to this issue, the parties generally agree that the "level of export subsidies" relevant to the analysis in this dispute is the overall level of Brazil's export subsidies. Although we do not decide that the overall level is the *only* possible basis for an examination of this issue, we do not see any reason to conclude that an analysis of the overall level of export subsidies is not *an* appropriate measure for the purposes of Article 27.4. The parties further agree that two programmes, PROEX and BEFIEX, are the only Brazilian export subsidy programmes relevant to this analysis. There is no information in the record before us suggesting the existence of export subsidies within the meaning of Article 3.1(a) of the SCM Agreement other than those provided pursuant to PROEX and BEFIEX. Accordingly, we will in this dispute examine the overall level of export subsidies provided by Brazil, i.e., the overall level of export subsidies provided under PROEX and BEFIEX.

7.60. The parties differ in one respect with respect to this issue. Canada contends that, because agricultural export subsidies are subject to special rules and separate reduction commitments under the Agreement on Agriculture, and because Article 13(c) of that Agreement exempts agricultural export subsidies that fully conform to Part V of that Agreement from the SCM Agreement's prohibition on export subsidies, such subsidies should be excluded in calculating the level of export subsidies under Article 27.4. Brazil disagrees, noting that Article 27 itself makes no distinction between agricultural and industrial subsidies. Brazil states, however, that neither PROEX nor BEFIEX are agricultural export subsidies, nor are they granted for the benefit of agricultural products. Canada has not contested Brazil's statements in this regard. Under these circumstances, we need not and do not decide whether the level of a Member's export subsidies within the meaning of Article 27.4 includes agricultural export subsidies.

7.61. The parties disagree as to the benchmark period against which an examination as to whether a Member has increased the level of its export subsidies should be made. Brazil asserts that, in the circumstances of this dispute, the appropriate benchmark is 1991, as that is the year in which the PROEX programme was first enacted. Canada considers that the relevant benchmark is 1994, as the condition in Article 27.4 not to increase the level of one's export subsidies became effective on 1 January 1995. We agree with Canada. The WTO Agreement entered into force on 1 January 1995. Article 27.2(b) allows developing country Members to maintain export subsidies for eight years from the date of entry into force of the WTO Agreement, provided they comply with the requirement of Article 27.4 that they not increase the level of their export subsidies during that period. Thus, logic would suggest that the appropriate reference period is the level of export subsidies in the period immediately preceding the date of entry into force.

7.62. The foregoing interpretation is confirmed by footnote 55. Footnote 55 provides that, "[f]or a developing country Member not granting export subsidies *as of the date of entry into force of the WTO*

Agreement, this paragraph shall apply on the basis of the level of export subsidies granted in 1986." Footnote 55 would appear to recognize that it would be inappropriate to impose on developing country Members which had before the entry into force of the WTO Agreement autonomously eliminated their export subsidies without a multilateral obligation to do so an obligation not to increase the level of its export subsidies above a zero level. Rather, it offers for such Members a ceiling level of export subsidies based on their 1986 level. Implicit in this explanation is that, absent footnote 55, a developing country Member which granted no export subsidies *as of the date of entry into force of the WTO Agreement* would be prohibited from providing any export subsidies during the eight-year transition period. Thus, footnote 55 indicates that the relevant benchmark period against which the obligation not to increase the level of export subsidies should be measured is a period immediately preceding the date of entry into force of the WTO Agreement.

7.63. Nor has Brazil offered any cogent reason why the Panel should use the year 1991 as a benchmark. We note that the sole stated basis for Brazil's view that we should look to 1991 rather than 1994 as the benchmark period is that 1991 is the year in which the PROEX programme was created. Given the agreement of the parties that the level of export subsidies in this dispute should relate to the overall level of Brazil's export subsidies, and not to the level of PROEX export subsidies alone, we fail to understand why the date on which PROEX was created should be relevant to our choice of a benchmark period. In the circumstances of this dispute, it would be equally logical – or illogical -- to use the date on which BEFIEX was enacted as the benchmark period.

7.64. Brazil contends that, if the Panel chooses not to use 1991 as a benchmark period, it should at least use a weighted average of the three or four years prior to the date of entry into force as the relevant period. It argues that such a benchmark would help reduce the distortion of the impact of a single year on the volatile economies of developing country Members. Once again, however, we consider that footnote 55 gives us useful guidance by providing at least a presumptive period for use as a benchmark. Footnote 55 provides for the use of "the level of export subsidies granted in 1986" when the developing country Member was not granting export subsidies as of the date of entry into force of the WTO Agreement. In other words, footnote 55 envisions using a one-year period as a benchmark for determining a developing country Member's level of export subsidies. Under these circumstances, and in the absence of any compelling reason to deviate from the approach suggested by footnote 55, we consider that it would be most appropriate in this case to use the single calendar year 1994 for the purpose of this analysis.

7.65. The parties also disagree vigorously with respect to whether, when considering the level of export subsidies, the Panel should examine budgeted amounts or actual expenditures. Canada contends that the level of export subsidies should be assessed by reference to actual expenditures, while Brazil contends that budgeted amounts represent the appropriate basis for the calculation. We agree with Canada. In our view, the level of a Member's export subsidies in its ordinary meaning refers to the level of subsidies actually provided, not the level of subsidies which a Member planned or authorized its government to provide through its budgetary process. This reading is in our view confirmed by footnote 55, which provides that, "[f]or a developing country Member not *granting* export subsidies as of the date of entry into force of the WTO Agreement, this paragraph shall apply on the basis of the level of export subsidies *granted* in 1986." (emphasis added). The verb "grant" has been defined to mean, *inter alia*, "to bestow by a formal act"²¹⁸ and "give, bestow, confer".²¹⁹ Thus, the verb "grant" in its ordinary meaning implies the actual provision of a subsidy, not its mere budgeting.²²⁰ Accordingly, the SCM Agreement envisions that

²¹⁸ *Shorter Oxford English Dictionary* (third edition).

²¹⁹ *Webster's Third New International Dictionary*.

²²⁰ Brazil defines "grant", without citation, as meaning "to agree, consent" or "to promise, undertake (which means 'to give formal promise or pledge')". Brazil further argues that the Portuguese term "dotação orçamentária" signifies a formal, legal

the proper point of reference in determining whether a Member has increased the level of its export subsidies is expenditures rather than budgeted amounts.

7.66. Brazil argues that "budgeted amounts, rather than expenditures, are the proper basis of comparison because they are the responsibility of the Member governments of the WTO." It contends that under the expenditure approach, a Member could increase its budgetary amounts and meet the requirements of Article 27.4 if the private sector did not fully utilise the budgeted sum, or fall out of compliance if the private sector utilised a sufficiently larger share of a smaller budgeted amount. We do not find these arguments compelling. A Member should be aware of the level of its past expenditures for export subsidies. If that Member budgets a larger amount than the amount it expended on export subsidies in a prior period, it should not be surprised if the private sector utilises that budgeted amount and as a result the Member is deemed to have increased the level of its export subsidies. On the other hand, if a Member increases the amount budgeted for export subsidies it may be that the Member intended to increase the level of its export subsidies, but that does not mean that it has actually increased the level of its export subsidies. In this respect, we agree with Canada that an expenditure-based measurement is consistent with the object and purpose of the SCM Agreement, which is to reduce economic distortions caused by subsidies. It seems to us that an increase in the level of export subsidies budgeted, which increase is not in fact actually realized, represents no more than a failed attempt by the subsidizing Member to increase the level of its export subsidies. That failed attempt in itself does not affect the interests of other Members.

7.67. As noted in paragraph 7.13 above, the parties disagree about the form of the financial contribution involved in this dispute, an issue which they consider has implications with respect to the question of when PROEX payments should be considered to have been "granted" for the purposes of calculating the level of Brazil's export subsidies in terms of expenditures. In Canada's view, PROEX payments involve a direct transfer of funds within the meaning of Article 1.1(a)(1) which occurs either when payments are made pursuant to a NTN-1 bond (i.e., where the lender redeems the bonds) or, in the alternative, when NTN-1 bonds are issued to an agent bank. Brazil, argues, to the contrary, that PROEX interest rate equalization in the first instance involve a potential direct transfer of funds which occurs at the moment that a letter is issued by the Export Credit Committee committing PROEX to provide interest rate equalization support for a transaction, provided that it is entered into according to the terms and conditions specified in a request for approval.

7.68. We recall that Article 1.1(a)(1) of the SCM Agreement provides that there is a financial contribution where, *inter alia*:

"a government practice involves a direct transfer of funds (e.g., grants, loans and equity infusion), potential direct transfer of funds or liabilities (e.g., loan guarantees)."

We believe that a "potential direct transfer of funds" exists only where the action in question gives rise to a benefit and thus confers a subsidy irrespective of whether any payment occurs. In arriving at this view, we have taken contextual guidance from the example of loan guarantees provided in Article 1.1(a)(1) of the SCM Agreement. Whether or not a loan guarantee confers a subsidy does not depend upon whether a payment occurs (i.e., whether the beneficiary of the guarantee defaults and the government is required to

binding promise – not an estimate – to the Brazilian exporter or financial institution to provide funds earmarked for PROEX in the budget, on a first-come, first-served basis, until the appropriated resources are depleted. While the verb "grant" may have a variety of meanings depending the context in which it is used, it is clear to us that, in the context of the phrase "export subsidies granted in 1986", the meanings cited by Brazil are inapposite, and it cannot reasonably be contended that a subsidy is "granted" merely because the government makes a budgetary authorization.

make good on the guarantee). For example, Article 14 of the SCM Agreement provides that, when examining benefit to the recipient in a countervail context, "a loan guarantee by a government shall not be considered as conferring a benefit, unless there is a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that a firm would pay on a comparable commercial loan absent the government guarantee." Thus, whether or not a loan guarantee confers a benefit depends on its effects on the terms of the loan and not on whether there is a default. Similarly, whether an export credit guarantee programme is an export subsidy under item (j) of the Illustrative List of Export Subsidies depends upon the premium rates charged and not upon whether a subsequent default occurs. While loan guarantees clearly are only one example of a "potential direct transfer of funds", we consider that other measures must share this basic characteristic in order to fall within that category of financial contribution.

7.69. In our view, if the category of potential direct transfers of funds referred simply to the situation where a government may in the future make a payment, almost any direct transfer of funds could, at an earlier date, be qualified as a potential direct transfer of funds. Nor do we see any reason to believe that a possible future payment is a "potential direct transfer of funds" merely because of a high probability that a payment will actually occur. The word "potential" has been defined as "possible as opposed to actual" or "capable of coming into being".²²¹ If the determination whether a measure was a "potential direct transfer of funds" depended upon the degree of likelihood or probability that a payment would subsequently occur, then the drafters surely would have chosen an adjective more suggestive of high probability than "potential."

7.70. Applying this approach to the case at hand, we recall Brazil's view that the issuance of a letter of commitment constitutes a potential direct transfer of funds. In this case, however, it clearly is not the alleged "potential direct transfer of funds", i.e., the letter of commitment, that confers the benefit. Rather, the benefit in the PROEX interest rate equalization scheme derives from the fact that a payment, i.e., a direct transfer of funds, has been or will be made. Brazil argues a potential direct transfer of funds exists here because Brazil is legally obligated under the letter of commitment to provide PROEX interest equalization payments *if* the export transaction to which the letter of commitment relates is concluded on the terms set forth in the request letter.²²² As explained above, the existence of a "potential direct transfer of funds" does not depend upon the probability that a payment will subsequently occur. Rather, the issue of whether and to what extent Brazil has taken a legal commitment to provide PROEX payments is relevant to determining *when* Brazil can be considered to have provided a *direct transfer of funds* in the form of a PROEX payment.

7.71. At what point in time can Brazil be considered to "grant" PROEX payments in the form of "direct transfers of funds"? As noted above, the verb "grant" has been defined to mean, *inter alia*, "to bestow by formal act" and "give, bestow, confer". Arguably, therefore PROEX payments may be "granted" where the unconditional legal right of the beneficiary to receive the payments has arisen, even if the payments themselves have not yet occurred. It is clear to us, however, that PROEX payments have not yet been "granted" at the time a letter of commitment is issued. We note that the issuance of a letter of commitment, even if legally binding on the Government of Brazil in the event certain conditions are fulfilled, provides no assurance that PROEX payments will actually be made. To the contrary, at the time the letter of commitment is issued no export sales contract has been signed, and the letter of commitment expires if a contract that conforms to the request for approval is not negotiated and signed within 90 days.

²²¹ *Shorter Oxford English Dictionary* (third edition).

²²² Brazil submitted a legal opinion prepared by a Brazilian lawyer for the proposition that the Government of Brazil cannot under Brazilian law annul or revoke a letter of commitment, once issued. *Legal Opinion from Professor Luiz Olavo Baptista*, Brazil exhibit 17.

Even the signing of a contract within that period does not trigger the issuance of bonds; in fact, business confidential information submitted by Brazil confirms that letters of commitment are issued with respect to options as well as firm contracts, which options may never be exercised. Rather, the right to receive the PROEX payments only arises after the conditions relating to receipt of PROEX payments, and specifically the condition that the product in question actually be exported, has been fulfilled. Thus, NTN-1 bonds are only issued if and when the aircraft whose financing is being supported by the interest rate equalization is actually exported. Accordingly, at the time the letter of commitment is issued, no PROEX payments have been made, nor has the beneficiary earned the unconditional right to receive PROEX payments. Rather, the issuance of the letter of commitment means only that, if an export transaction is closed within a certain period of time, and if the product in question actually is exported, a right to receive PROEX payments will arise.

7.72. The question remains whether PROEX payments are "granted" when the bonds are issued or whether they are granted only when the bonds are redeemed on a semiannual basis. In our view, PROEX payments should be considered to be "granted" when bonds are issued and title to those bonds is transferred to the lender financial institution. In this respect, we note that the terms "funds" is defined as, *inter alia*, "pecuniary resources". The word "pecuniary", in turn, is defined as, *inter alia*, "of, belonging to, or having relation to money".²²³ Thus, the term "funds" can be defined to mean "resources of, belonging to, or having relation to money". It is true that the bonds are not fully equivalent to money, in that they can only be redeemed at some future date. Nevertheless, we consider that the transfer of title of these bonds to the lender should be considered to be the moment that a direct transfer of funds occurs. In this respect, we note that, while the bonds cannot be immediately redeemed, they are freely negotiable.²²⁴ The parties agree that lenders may exercise their right to sell these bonds – albeit at a discount as determined by the market -- to other entities rather than waiting until maturity to redeem the bonds themselves. Thus, at the point that title to the bonds is passed to the lenders, those lenders are the holders of a property right with a market value which is immediately realisable. Accordingly, we conclude that PROEX payments are "granted" at that point, and we will calculate the Brazil's PROEX expenditures on that basis.

7.73. Finally, we note that, while the parties appear to agree that "the level of export subsidies" should be measured in US dollars in this case, they disagree as to whether the level should be expressed in constant or nominal dollars. Brazil argues that it is logical to use a constant point of comparison to measure the level of a developing country Member's export subsidies. Canada responds that there is no indication in Article 27.4 that adjustment should be made for inflation, and that in cases – such as Annex IV:5 to the SCM Agreement -- where the drafters considered that an inflation adjustment was appropriate, they specifically provided for it. In our view, however, it is appropriate in this case to use constant dollars, as that will provide a more meaningful assessment as to whether Brazil has increased the level of its export subsidies. We note that, in this case, the conclusion with respect to this issue would be the same whether constant or nominal dollars are used.

7.74. In conclusion, we consider that the level of Brazil's export subsidies should be appropriately measured in this case by reference to Brazil's overall level of export subsidies, which the parties agree consist of PROEX and BEFIEX subsidies. We further consider that the proper measure of the level of Brazil's export subsidies is the level of its expenditures, not its budgeted amounts, and that the proper benchmark period against which to examine whether that level has increased is calendar year 1994. We see no reason not to measure the level in US dollars, consistent with the data submitted by both parties.

²²³ *Shorter Oxford English Dictionary* (third edition).

²²⁴ Ministry Order Nos. 121/97 of 12 August 1997 and 18/98 of 27 January 1998.

7.75. There is no factual dispute among the parties regarding the evidence submitted to the Panel regarding the level of Brazil's export subsidies. The data which are relevant in light of our legal analysis are reflected in Table 9:

TABLE 9

**Brazilian Export Subsidies
(PROEX and BEFIEX)**

	Total Expenditures* (current US\$)	Total Expenditures (1994 constant US\$)
1994	339.6	340
1995	269.5	263
1996	286.7	275
1997	412.5	389
1998**	537.8	502

Source: Brazil exhibit 20.

* PROEX payments appear as expenditures in the year the bonds are issued.

** PROEX expenditures January-October.

Applying the foregoing criteria to these undisputed data, we conclude that Brazil had by 1997 increased the level of its export subsidies above that prevailing in 1994, whether the data are expressed in nominal or in constant dollars. The increase for 1998 was even more substantial than that for 1997, reflecting as it does data for only the first ten months of the year.

7.76. For the foregoing reasons, we conclude that Brazil has "increased the level of its export subsidies" within the meaning of Article 27.4 of the SCM Agreement.

4. Has Brazil complied with the condition that it "phase out its export subsidies within the eight-year period"?

7.77. Canada contends that, under Article 27.4, a developing country Member seeking to benefit from the non-application of the Article 3.1(a) prohibition must phase out its export subsidies within eight years from the date of entry into force of the WTO Agreement. In Canada's view, this provision reflects two requirements. First, a developing country is required to "bring gradually out of use", its export subsidies during the eight-year period. Second, the developing country Member is required to terminate its export subsidies by the end of the eight-year period. In Canada's view, Brazil has failed to comply with either condition.²²⁵

7.78. We note, first, that there can be no question, and Brazil does not contest, that a developing country Member other than one referred to in Annex VII is as a general rule required by Articles 27.2(b) and 27.4 to eliminate its export subsidies within eight years from the date of entry into force of the WTO Agreement. We further note, however, that Article 27.4 envisions that an extension of that period may be granted on request of the developing country Member if the Committee on Subsidies and Countervailing Measures determines that an extension of the period is justified, after examining all the relevant

²²⁵ It could also be argued that the "phase out" obligation entails a requirement not to increase the level of a Member's export subsidies. In light of our findings with respect to the explicit requirement of Article 27.4 that a Member not increase the level of its export subsidies, we need not consider this matter further.

economic, financial, and development needs of the developing country Member. We further consider it evident that any such extension granted by the Committee would effectively extend the eight-year period specified in Article 27.2(b) and would render the prohibition on export subsidies under Article 3.1(a) inapplicable for the period for which the extension was granted (assuming the developing country Member continued to comply with the other conditions found in Article 27.4).

7.79. With respect to a developing country Member's obligations during the eight-year period, Article 27.4 provides that "[a]ny developing country Member referred to in paragraph 2(b) shall phase out its export subsidies, preferably in a progressive manner." We agree with Canada that the "principal interpretive challenge" presented by this provision is the need to reconcile the *mandatory* language providing that a developing country Member "shall phase out its export subsidies" with the hortatory language in the final clause encouraging Members to perform their phase-out in a progressive manner. In its ordinary meaning, the term "phase out" means, *inter alia*, "to discontinue the practice, production or use of by phases."²²⁶ Thus, Article 27.4 appears to require the phased elimination of export subsidies within the eight-year period. On the other hand, Article 27.4 provides that the phase out should "preferably" be performed in a progressive manner. The word "progressive" has been defined as "proceeding step by step, occurring one after another, successive".²²⁷ Brazil argues, not without some reason, that the term "phase out" should not be interpreted to *require* the phased elimination of export subsidies when the subsequent clause indicates that phased elimination is not required but only preferred. Canada responds that the tension between these two phrases can be reconciled if the term progressive is defined, as in the context of tax rates, to mean that a Member should phase out its export subsidies "at an increasing pace". Under this interpretation, a developing country would be required to undertake a phased elimination of its export subsidies, and would be encouraged, but not required, to reduce its subsidies at an increasing rate.

7.80. The parties have in this dispute identified what could be viewed as an internal contradiction within the text of Article 27.4. Brazil suggests that the term "phase out" must be read in the context of the subsequent clause and thus not be interpreted to require phased elimination. This however requires ascribing to the term "phase out" a meaning which is more limited than its ordinary meaning. Canada on the other hand has suggested a reading of the text which would eliminate the contradiction, but which relies upon ascribing a highly particularised meaning to the word "progressive". In fact, although Canada indicates that "progressive" may mean "at an increasing rate", it cites no dictionary in support of that definition. Further, Canada has cited no logical reason why the drafters would express a non-binding preference for an end-loaded phased elimination of export subsidies by developing country Members. Rather, given that the object and purpose of the SCM Agreement is to impose multilateral disciplines on trade-distorting subsidization, one would expect that any preference would be for a front-loaded, rather than an end-loaded, phase-out. Accordingly, the Canadian interpretation would have us ascribe a special meaning to the term "progressive" without any support, either direct or circumstantial, that the drafters so intended. Thus, neither the Canadian nor the Brazilian approach is entirely satisfactory from a legal perspective.²²⁸

²²⁶ *Webster's Third International Dictionary*.

²²⁷ *Shorter Oxford English Dictionary* (third edition).

²²⁸ Although neither party has referred to the Spanish or French texts, we note that they would tend to support the Brazilian interpretation. Thus, the Spanish text provides that "Los países en desarrollo Miembros a que se refiere el párrafo 2 b) eliminarán sus subvenciones a la exportación dentro del mencionado período de ocho años, preferentemente de manera progresiva." The French text provides that "Tout pays en développement Membre visé au paragraphe 2 b) supprimera ses subventions à la exportation dans le délai de huit ans, de préférence de façon progressive." The terms "eliminarán" and "suprimera" do not bear the suggestion of "phased elimination" suggested by the English term "phase out".

7.81. Although the issue identified above is an interesting and complex one, we do not consider that we need resolve it in the context of this dispute. In our view, even if the term "phase out" does require the phased elimination of export subsidies by a developing country Member within the eight-year period, it does not specify in how many phases the elimination should be carried out, what the time-period between these phased reductions should be, and how these phased reductions should be distributed within the eight-year period.²²⁹ We acknowledge that Brazil has not to date carried out any phased reductions in the level of its export subsidies, and that there is nothing in the record indicating that Brazil at the moment has any intention to do so. Thus, it may be said that it is possible, or even highly likely, that Brazil will not engage in phased reductions in its export subsidies within the eight-year period. Nevertheless, we cannot preclude that Brazil will engage in phased reductions between now and 31 December 2002. Accordingly, we cannot conclude on the basis of Brazil's actions in the first four years since the date of entry into force of the WTO Agreement that Brazil has failed to comply with the phase-out requirement of Article 27.4 by reason of a failure to undertake phased reductions within the eight-year transition period.²³⁰

7.82. The question remains whether Brazil has failed to comply with the phase-out requirement of Article 27.4 by reason of an alleged failure to eliminate its export subsidies by the end of the eight-year period. In this respect, Canada submits that PROEX does not have a termination date; that the financing period provided for regional aircraft under PROEX interest rate equalization is from ten to fifteen years; and that various purchasers have firm orders or options for aircraft to be delivered "well after 1 January 2003" on which they expect to receive PROEX payments. With respect to the latter contention, Canada cited a press report and a study indicating that at least one carrier benefiting from PROEX interest rate equalization is expected to continue taking delivery of Brazilian regional jets into the year 2004. Canada further argues that, comparing EMBRAER's current firm orders and options to its production schedule, EMBRAER must be reserving delivery slots beyond 2002 for existing customers, and that, "to the extent that these airlines expect to receive PROEX export subsidies", Brazil is not complying with its obligation to phase out its export subsidies by the end of the eight-year period.

7.83. Turning first to Canada's argument that PROEX does not have a termination date, we do not consider that the absence of a termination date for PROEX demonstrates that Brazil is not in compliance with its obligation to eliminate its export subsidies by the end of the eight-year period. In this respect, we do not agree with Canada that,

"in order to establish its conformity with the 'phase out' Brazil must, at the very least, demonstrate that it has put in place a programme or a schedule of phased reductions of its export subsidies, with a view to elimination at the end of the grace period." (emphasis in original).²³¹

While developing country Members certainly would be well advised to plan as far as possible in advance for the elimination of their export subsidies, their failure to do so does not in itself demonstrate that the

²²⁹ It is instructive in this respect to compare, for example, the highly detailed provisions regarding the phased integration into GATT 1994 of textile and clothing products in Article 2 of the Agreement on Textiles and Clothing.

²³⁰ We note that the definition of "phase out" cited by Canada is "to bring gradually . . . out of use", and that gradually has been defined as taking place "by degrees, slowly progressive, not rapid, steep or abrupt". Canada deduces from this that Brazil's obligation is not only to "bring its export subsidies out of use in a phased manner" but also to show that it "does not intend to bring its subsidies to a 'rapid, steep or abrupt end' before the end of the eight-year period." We do not consider however that in the absence of more precise requirements we can reasonably infer into the term "phase out" any more than an obligation to bring one's export subsidies out of use in a phased manner.

²³¹ Canada answer to Panel question 49.

required elimination will not occur. Nor does the fact that PROEX interest rate equalization has been provided with respect to financing extending beyond the 31 December 2002 in our view warrant a different conclusion. As discussed in paragraph 7.72, above, we consider that a PROEX interest rate equalization subsidy is granted at the moment that title to the bonds relating to the equalization is transferred to the lender financial institution. Accordingly, the relevant question in our view is not whether bonds issued before the end of the transition period may be redeemed after the end of that period, but rather whether Brazil continues to issue new bonds – and therefore to grant further subsidies – after the end of the transition period. It is to this issue that we now turn.

7.84. As noted in paragraph 7.82 above, Canada relies upon a press report²³² and estimates in a study²³³, as well as calculations based on EMBRAER's order book and production schedule, for the proposition that Brazil has already committed to provide PROEX interest rate equalization with respect to regional aircraft that will be delivered after 31 December 2002.²³⁴ The most telling evidence is the press report, which states that "Eagle expects to take delivery of its first ERJ-135 in July of next year, and continue accepting airplanes through 2004". Brazil concedes that this transaction involves PROEX interest rate equalization.²³⁵ Further, Brazil has argued forcefully that it is legally required, as of the date that it issues a letter of commitment to EMBRAER, to issue the bonds if the terms of the letter of commitment are respected.²³⁶ Because, under the PROEX interest rate equalization scheme, bonds relating to an export transaction are not issued until it has been confirmed that an export transaction will in fact occur,²³⁷ this strongly suggests that Brazil will continue to issue bonds – and hence to grant new subsidies – after 31 December 2002. Accordingly, Canada has established in our view that Brazil will continue to issue bonds, and thus to grant PROEX interest rate equalization subsidies – although at a level which cannot be determined -- beyond 31 December 2002.

7.85. Is the foregoing demonstration sufficient to show, in advance, that Brazil has not complied with the condition of Article 27.4 that it "phase out its export subsidies within the eight-year period"? We consider that it is. It is true, as we stated above,²³⁸ that the Committee on Subsidies and Countervailing Measures may extend the eight-year period, and that during the period of any such extension the Article 3.1(a) prohibition on export subsidies would continue to be inapplicable to the developing country Member in question. Brazil, however, has entered into a legally binding commitment to issue bonds where certain conditions are met without having yet even requested an extension of that period. Further, we note that this commitment has had an effect on the marketplace by allowing EMBRAER to conclude export contracts for deliveries of regional aircraft to occur, and for subsidies to be granted, after the end of that period. Accordingly, we must conclude on the facts before us that Brazil has not complied with its obligation to phase out its export subsidies by the end of the transition period.

²³² See *American Eagle to Replace Aging Saabs with ERJ-135s*, in *Flight International*, 1 October 1998 (Canada exhibit 71).

²³³ See Canada exhibit 64.

²³⁴ Although this evidence may be less than conclusive, we consider it sufficient to raise a presumption that Canada's factual assertion is correct, particularly in light of the fact that access to definitive information on this issue is in the sole possession of Brazil and the companies in question, and that Brazil has at no point not contested the accuracy of Canada's assertions in this regard.

²³⁵ See Brazil submission "Comments on Additional Information Submitted by Canada", paragraph 26.

²³⁶ According to a written legal opinion submitted by Brazil to the Panel, "it is our opinion that, within the validity period of the letters of commitment and provided there are no pending debts from the exporter to the GOB, it is illegal and not viable the cancellation or the revoking of the interest rate equalization concessions made for the referred to transactions." *Legal Opinion from Professor Luiz Olavo Baptista*, Brazil exhibit 17.

²³⁷ According to Brazil, where there is confirmation of the shipment of goods or the effective settlement of the relevant foreign exchange contract for the aircraft in question. See Brazil's answer to Panel question 28.

²³⁸ Paragraph 7.82.

7.86. For the foregoing reasons, we find that Brazil has failed to comply with the condition of Article 27.4 relating to the phase out of its export subsidies.

5. Are Brazil's export subsidies "inconsistent with its development needs"?

7.87. Canada considers that, under the second sentence of Article 27.4, a developing country Member seeking to benefit from non-application of the Article 3.1(a) prohibition on export subsidies must demonstrate that its export subsidies are consistent with its development needs. Canada considers that this is not a self-judging provision, and that it should be applied on the basis of objective standards. Although Canada "does not propose to set out these standards", it does argue that one objective standard in this case consists of the domestic content standards established by Brazil with respect to PROEX. Specifically, Canada argues that with respect to regional aircraft Brazil has waived the domestic content rules generally applicable under PROEX and provides interest rate equalization on the full value of the aircraft in spite of the low domestic content of those aircraft. Canada argues that another relevant standard may be foreign exchange earnings versus foreign exchange expenditure on export subsidies.

7.88. Brazil argues that Article 27 presumes that export subsidies are consistent with a developing country Member's development needs. In support of this view, it cites Article 27.1 of the SCM Agreement, which provides that "Members recognize that that subsidies may play an important role in economic development programmes of developing country Members." Brazil further argues that the language of Article 27.4, which provides that export subsidies shall be eliminated in a period shorter than eight years "when the use of subsidies is inconsistent with" a developing country Member's development needs, clearly means that the burden is on the challenging Member to demonstrate the "inconsistency". Brazil rejects Canada's view that the waiver of certain domestic content regulations in the case of PROEX interest rate equalization payments for regional aircraft is relevant: Article 27 contains no domestic content requirement, and any standards applied with respect to this issue should in Brazil's view relate to the overall needs of the developing country Member, not to one particular industry or economic sector. Finally, Brazil asserts on the basis of certain information regarding economic conditions and the importance of an open, export-oriented economy that PROEX is in fact consistent with its development needs.

7.89. In considering this issue, we note that this element of Article 27.4 is troubling from the perspective of a panel. Article 27.4 provides in relevant part that a developing country Member "shall eliminate [its export subsidies] within a period shorter than that provided for in this paragraph when the use of such export subsidies is inconsistent with its development needs." We recognize that as written this clause is mandatory, and a conclusion that this clause was not susceptible of application by a panel would be inconsistent with the principle of effective treaty interpretation. On the other hand, an examination as to whether export subsidies are inconsistent with a developing country Member's development needs is an inquiry of a peculiarly economic and political nature, and notably ill-suited to review by a panel whose function is fundamentally legal.²³⁹ Further, the SCM Agreement provides panels with no guidance with respect to the criteria to be applied in performing this examination. We consider that it is the developing country Member itself which is best positioned to identify its development needs and to assess whether its export subsidies are consistent with those needs. Thus, in applying this provision we consider that panels should give substantial deference to the views of the developing country Member in question.

²³⁹ It may be noted that under Article 27.14, "[t]he Committee [on Subsidies and Countervailing Measures] shall, upon request by an interested Member, undertake a review of a specific export subsidy practice of a developing country Member to examine whether the practice is in conformity with its development needs." In our view, a body such as the Committee is far better equipped to perform this type of examination than is a panel.

7.90. As discussed above, we consider that Canada bears the burden of demonstrating that, because Brazil has not complied with the conditions set forth in Article 27.4, the Article 3.1(a) prohibition on export subsidies applies to Brazil. Further, we note that Article 27.4 does not provide that a developing country Member must eliminate its export subsidies in a period shorter than eight years *unless* the use of such export subsidies *is consistent* with its development needs. Rather, it provides that a developing country Member must eliminate its export subsidies in a period shorter than eight years *if* the use of such export subsidies is *inconsistent* with its development needs. Thus, in order to prevail on this issue Canada must present evidence and argument sufficient to raise a presumption that the use of export subsidies by Brazil is inconsistent with Brazil's development needs.

7.91. Canada argues that PROEX payments on exports of regional aircraft are inconsistent with Brazil's development needs because Brazil has waived certain domestic content rules generally applicable under PROEX in the context of the export of such regional aircraft. Specifically, Canada asserts that under PROEX regulations, exports with a domestic content index of 60 per cent or more are subject to interest rate equalization payments on 100 per cent of their value, while for goods with a domestic content index of less than 60 per cent, the percentage eligible for interest rate equalization is reduced according to a formula. Canada asserts that the ERJ-145 regional jet, for example, has a domestic content index of approximately 15 per cent, and thus should be eligible for interest rate equalization on only 55 per cent of its value, but that it in fact benefits from 100 per cent equalization. Canada further notes that the spare parts may make up as much as thirty per cent of the value of the export package, and that these spare parts could have no Brazilian content whatsoever. Brazil has not contested Canada's calculations of the Brazilian value-added of the ERJ-145, nor its characterization of PROEX domestic content rules.²⁴⁰

7.92. It is not entirely clear whether under Article 27.4 it is a particular export subsidy practice or a Member's export subsidies generally which must be shown to be inconsistent with its development needs.²⁴¹ Even if we assume that it is appropriate to review whether a particular subsidy practice with respect to a particular product is inconsistent with a developing country Member's development needs, we do not believe that the evidence submitted by Canada is sufficient to raise a presumption that PROEX payments on regional aircraft are inconsistent with Brazil's development needs. In our view, the fact that Brazil has a generally applicable rule regarding the relationship between the domestic content of an exported product and the extent of the PROEX interest rate equalization available with respect to that product does not mean that the deviation from that rule in a particular case is necessarily inconsistent with a developing country Member's development needs. Nor do we see any basis to conclude that PROEX payments on regional aircraft are necessarily inconsistent with Brazil's development needs merely because the Brazilian value-added of the aircraft being exported is relatively low. There could be any number of reasons why the provision of export subsidies might be consistent with a Member's development needs in such a case. For example, a developing country Member might be interested in the possible technological spin-off effects from the development and production of the product in question, or

²⁴⁰ Canada's calculations appear to be based on a study performed by Ernst and Young on behalf of Canada entitled *Analysis of EMBRAER's Use of the Brazilian Export Financing Program PROEX*. Although Canada did not submit this study into evidence, Brazil submitted it as exhibit 9 to support certain arguments of its own. On the basis of this study (p. 18), it appears that the domestic content figure cited by Canada in fact referred to the ERJ-135 (with an estimated Brazilian value-added of 14.8 per cent) rather than to the ERJ-145 (with an estimated Brazilian value-added of 26.1 per cent). We note however that business confidential documents submitted by Brazil indicate that in the view of the Bank of Brazil the domestic content of the ERJ-145 is substantially higher than estimated by Canada.

²⁴¹ Article 27.14 envisions the review by the Committee of whether a "specific export subsidy practice" by a developing country Member is in conformity with its development needs. This language differs notably from that of Article 27.4, which refers merely to "such export subsidies", with "such" presumably referring back to the export subsidies whose level a Member is not to increase (and recalling that, in this case at least, the "level of export subsidies" is being examined in terms of the overall level of export subsidies being provided by Brazil).

the need to establish a strong market presence and reputation in foreign markets as a stepping stone to introducing products with greater national value-added. In fact, Canada has not made any meaningful effort to relate the issue of Brazilian value-added to the broader issue of Brazilian development needs.²⁴²

7.93. For the foregoing reasons, we conclude that Canada has failed to present evidence and argument sufficient to raise a presumption that the use of export subsidies by Brazil is inconsistent with Brazil's development needs.

VIII. CONCLUSIONS AND RECOMMENDATION

8.1. In conclusion, we find that:

(a) PROEX interest rate equalization payments on exports of Brazilian regional aircraft are subsidies within the meaning of Article 1 of the SCM Agreement which are contingent upon export performance within the meaning of Article 3.1(a) of that Agreement;

(b) PROEX interest rate equalization payments on exports of Brazilian regional aircraft are not "permitted" by reason of the first paragraph of item (k) of the Illustrative List of Export Subsidies;

(c) Brazil has failed to comply with certain of the conditions of Article 27.4 of the SCM Agreement and the prohibition of Article 3.1(a) of the SCM Agreement is therefore applicable to Brazil.

8.2. Accordingly, we find that payments on exports of regional aircraft under the PROEX interest rate equalization scheme are export subsidies inconsistent with Article 3 of the SCM Agreement.

8.3. Pursuant to Article 3.8 of the DSU, the finding in paragraph 8.2 also constitutes a case of *prima facie* nullification or impairment of benefits accruing to Canada under the SCM Agreement, which Brazil has not rebutted.

8.4. Canada has requested that the Panel make specific recommendations regarding implementation of these findings. We consider however that we are required to make the recommendation provided for in Article 4.7 of the SCM Agreement and are authorized to make no other. Accordingly, we recommend that Brazil withdraw the subsidies identified above without delay.

8.5. Article 4.7 further provides that "the panel shall specify in its recommendation the time-period within which the measure [i.e., the measure found to be a prohibited subsidy] must be withdrawn." Presumably, we are expected to take into account the nature of the measures and the difficulties likely to be faced in implementing the recommendation when specifying what period would represent withdrawal "without delay". We note, however, that there is no experience with respect to what steps could constitute "withdrawal" of the subsidies in various factual circumstances, and we do not consider that it is within our mandate to tell Brazil what steps are required in order to implement our recommendation. Accordingly, taking into account the nature of the measures and the procedures which may be required to implement our recommendation, on the one hand, and the requirement that Brazil withdraw its subsidies "without delay" on the other, we conclude that Brazil shall withdraw the subsidies within 90 days.

²⁴² In light of our view that the evidence submitted by Canada is insufficient to raise a presumption that PROEX payments are inconsistent with Brazil's development needs, we need not consider Brazil's response to Canada's assertions.