WORLD TRADE ORGANIZATION

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CANADA – MEASURES AFFECTING THE IMPORTATION OF MILK AND THE EXPORTATION OF DAIRY PRODUCTS

AB-1999-4

Report of the Appellate Body

WORLD TRADE ORGANIZATION
APPELLATE BODY

Canada – Measures Affecting the Exportation of Dairy Products and the Importation of Milk

Canada, *Appellant*

New Zealand, *Appellee*
United States, *Appellee*

AB-1999-4

Present:

Matsushita, Presiding Member
Feliciano, Member
Lacarte-Muró, Member

I. Introduction

1. Canada appeals from certain issues of law and legal interpretations developed by the Panel in *Canada – Measures Affecting the Importation of Milk and the Exportation of Dairy Products* (the "Panel Report").[1] Following their requests for consultations, the United States[2] and New Zealand[3] requested that the Dispute Settlement Body (the "DSB") establish panels to examine certain alleged export subsidies that they contended Canada or its provinces had granted, through the Special Milk Classes Scheme, to support the export of dairy products and to examine a claim by the United States regarding imports into Canada of fluid milk and cream within the 64,500 tonnes tariff-rate quota committed in Canada's Schedule of Commitments under the *Marrakesh Agreement Establishing the World Trade Organization* (the "*WTO Agreement*"). On 25 March 1998, the DSB agreed to establish two panels in accordance with these requests and further agreed that the two panels would be consolidated into a single panel pursuant to Article 9.1 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* (the "DSU") with standard terms of reference.

2. The Panel considered claims made by the United States and New Zealand that Canada's measures are inconsistent with Articles II, X, XI and XIII of the *General Agreement on Tariffs and Trade 1994* (the "GATT 1994"); Articles 3, 4, 8, 9, and 10 of the *Agreement on Agriculture*; Article 3 of the *Agreement on Subsidies and Countervailing Measures* (the "*SCM Agreement*"); and Articles 1, 2 and 3 of the *Agreement on Import Licensing Procedures*. The Panel Report was

[1]WT/DS103/R, WT/DS113/R, 17 May 1999.

[2]WT/DS103/4, 2 February 1998.

[3]WT/DS113/4, 12 March 1998.

circulated to Members

II. Background

A. *The Canadian Dairy Regime*

6. The relevant factual and regulatory aspects concerning the Canadian dairy regime, including the Special Milk Classes Scheme, are fully described in paragraphs 2.1 to 2.66 of the Panel Report. For the purposes of this appeal, we summarize certain of the principal aspects of the Panel's factual findings.

1. Institutions

7. Regulatory jurisdiction over trade in dairy products in Canada is divided between the federal and the provincial governments.[7] The Canadian federal government has the power to regulate inter-provincial and international trade generally, including trade in milk, while the provincial governments have jurisdiction over aspects of the production and sale of milk within the provinces.[8] Three entities have decision-making roles with respect to the production and sale of milk in Canada: the Canadian Dairy Commission (the "CDC"), the provincial milk marketing boards and the Canadian Milk Supply Management Committee (the "CMSMC").

(a) CDC

8. The CDC is a Crown corporation established under the Canadian Dairy Commission Act (the "CDC Act"), a federal statute.[9] The CDC is funded by the Canadian federal government as well as by its market activities y 9 erTw

respective provincial governments and is chaired by the CDC.[25] The Dairy Farmers of Canada, the

3. Price of Milk to the Processor

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III. Arguments of the Participants

A. *Claims of Error by Canada – Appellant*

1. Article 9.1(a) of the *Agreement on Agriculture*

(a) "direct subsidies, including payments-in-kind"

18. Canada contends that the interpretation of the term "export subsidies" in the *Agreement on Agriculture* must take into account the related provisions of the *SCM Agreement*. The *Agreement on Agriculture* and the *SCM Agreement* are both Multilateral Agreements on Trade in Goods and, in the language of Article II:2 of the *WTO Agreement*, are "integral parts" of the *WTO Agreement*. The two Agreements reflect the latest statement of WTO Members as to their rights and obligations concerning agricultural subsidies. The clear inference is that, if possible, there should be consistency of interpretation between the two Agreements, particularly with respect to the notions of "subsidies" and "export subsidies". In Canada's view, the Panel did not give proper consideration to this need for consistent interpretation.

19. Canada submits that the interpretation of the expression "direct subsidies, including payments-in-kind", in Article 9.1(a) of the *Agreement on Agriculture*, should begin with the word "subsidies". That word, although not defined in the *Agreement on Agriculture*, is defined in Article 1.1 of the *SCM Agreement*. If the elements identified in Article 1.1 are present, Article 9.1(a) of the *Agreement on Agriculture* requires examination of whether the "subsidies" are "direct". The Panel erred by failing to do this. In Canada's view, a subsidy is "direct" if: it is funded directly from government funds; it is paid directly to the beneficiary by the government itself; *and* it does not involve the activities of non-governmental actors acting through a government-mandated scheme. In this case, since the alleged subsidy is not funded by government, it is not "direct".

20. The Panel also erred by "equating 'payments-in-kind' with 'direct subsidies'".[41] A subsidy may take the form of a "payment-in-kind", but a "payment-in-kind" is not necessarily a "subsidy". By collapsing these separate legal concepts, the Panel failed to address the two fundamental elements of Article 9.1(a): namely, the terms "direct" and "subsidies".

[41]Canada's appellant's submission, para. 46.

21. Canada contends that the Panel also substituted for the ordinary meaning of "payments", in the term "payments-in-kind", a special meaning of "gratuitous act, a bounty or benefit".[42] The end

inaccuracies"[45], without providing a basic rationale under Article 12.7 of the DSU to justify placing reliance on such evidence.

(b) "governments or their agencies"

26. Canada argues that the Panel erred by finding that the provincial milk marketing boards are government agencies "solely on the basis of one characteristic: the delegation of some governmental authority."[46] The mere fact of delegation of authority from government is not sufficient to conclude that an entity is an agency of government.

27. Canada notes that, in Article 9.1(a), marketing boards are identified as potential recipients of "direct subsidies". The implication is that a marketing board is distinct from "governments or their agencies". Moreover, if marketing boards are deemed to be "government agencies", the result would be that subsidies are being provided by a government to itself.

28. According to Canada, the Panel was misguided in relying on Article XVII of the GATT 1994 to support its conclusion that marketing boards may be government agencies. That provision has no bearing on the status of the marketing boards at issue under Article 9.1(a). Similarly, the Panel's reference to Article XXIV:12 does not advance its reasoning. That provision states that "regional" or "local" authorities are subject to GATT obligations but does not define such authorities. eA Tc 0.3455oj 136.5 0 Trtic

31. Canada adds, finally, that the judgment in the *Bari III* case, referred to by the Panel, provides no support for the proposition that the provincial milk marketing boards should be deemed to be government agencies because they enjoy some delegated powers.

2. Article 9.1(c) of the *Agreement on Agriculture*

(a) "payments"

32. Canada contends that the Panel erred by collapsing the distinction between the term "payments" in Article 9.1(c) and the term "payments-in-kind" in Article 9.1(a). These words have different meanings: where the drafters intended the word "payments" to include "payments-in-kind", this was indicated in the text, as in the case of Article 9.1(a) and of paragraph 5 of Annex 2. The absence of an express reference to "payments-in-kind" in other provisions of the

milk will actually be produced. Canada also underlines the differences in the pooling of returns to producers as between in-quota and over-quota milk.

3. Article 10.1 of the *Agreement on Agriculture*

36. Canada observes that Article 10.1 applies to "subsidies contingent upon export performance", other than those subsidies listed in Article 9.1. The Panel erred by suggesting that the scope of the measures covered by Article 10.1 is drawn from the items listed in Article 9.1. The Panel indicated that a measure, which is partially, but not completely, covered by Article 9.1, should, for that reason, be included under Article 10.1. Canada emphasizes that a practice not included in Article 9.1 can only be an "export subsidy" if it satisfies the definition of that term in Article 1(e) of the

intended to restrict access to the tariff-rate quota to "cross-border purchases imported by Canadian consumers".

41. Canada submits that because the Panel failed to ascribe any substantive meaning to Canada's terms and conditions, the Panel also failed properly to interpret the meaning of the word "consumer" in the notation. As a result of its approach, the Panel failed to rule on the central issue, namely, whether Canada must permit commercial import shipments of fluid milk within the two tariff lines in question.

42. In view of the doubts regarding the interpretation of the notation, the Panel should have clarified the meaning by considering the negotiating history pursuant to Article 32 of the *Vienna Convention on the Law of Treaties* (the "*Vienna Convention*").[48] Canada asserts that it was clear from the record before the Panel that Canada proposed to maintain its existing access opportunities, unless the United States removed barriers to Canadian access to the United States' market. Those existing access opportunities did not extend to commercial imports.

B. *Arguments of New Zealand – Appellee*

1. Article 9.1(a) of the *Agreement on Agriculture*

(a) "direct subsidies, including payments-in-kind"

43. New Zealand disagrees with Canada's view that the export subsidy provisions of the *Agreement on Agriculture* and the *SCM Agreement* form a single, comprehensive statement and must, therefore, be interpreted consistently. Even though the *WTO Agreement* may constitute a single undertaking, that does not mean that the provisions of one part are to be governed by the

between them and this hierarchy must be respected. Furthermore, on Canada's argument, neither Agreement could be applied in isolation, since only by applying the Agreements together could

may be interpreted consistently. Even though the *Vienna*

45. New Zealand agrees with the Panel that provision of goods at a reduced price can constitute a "payment-in-kind". If processors were to purchase milk at a higher price and receive a rebate, the rebate would undoubtedly be a "payment". In the case of Special Classes 5(d) and 5(e), the rebate is

contends that both the *Ad* note to Article XVII:1, and Article XXIV:12 of GATT 1994 indicate that marketing boards are capable of being agencies of government, although neither purports to provide a universal definition of government agency.

51. New Zealand disagrees with Canada's argument on Item (d) of the Illustrative List. Item (d) says nothing about the "government" status of "government-mandated schemes" since Item (d) does not depend upon whether those schemes are governmental or non-governmental.

52. Finally, New Zealand contends that Canada's argument that the status of the provincial milk marketing boards should be determined by Canadian domestic law is contrary to Article 3.2 of the DSU, which provides that the WTO Agreements are to be interpreted "in accordance with customary rules of interpretation of public international law."

2. Article 9.1(c) of the *Agreement on Agriculture*

(a) "payments"

53. New Zealand maintains that the Panel properly applied the appropriate principles of treaty interpretation in its examination of the word "payments". A "payment-in-kind" is a *form* of payment. Canada has offered no substantive argument to show that this is wrong.

54. According to New Zealand, Canada's argument regarding revenue foregone suggests that such revenue would be excluded from the assessment of budgetary outlay commitments made for "export subsidies" under Article 9.1, unless there is explicit reference to revenue foregone in a particular sub-paragraph of Article 9.1. Since none of the sub-paragraphs in Article 9.1 refers specifically to revenue foregone, the implication of the Canadian argument is that revenue foregone need not be included at all in the calculation of "budgetary outlay" commitments. This is a rewriting of Articles 1(c), 9.1 and 9.2(a) of the *Agreement on Agriculture.*

(b) "financed by virtue of governmental action"

55. New Zealand submits that, for the reasons given in its arguments on the meaning of "governments or their agencies", the Panel's analysis under Article 9.1(c), insofar as it is based on its analysis under Article 9.1(a), is correct. Canada is attempting to reargue the facts of the case by focusing on differences between in-quota and over-quota milk that the Panel did not regard as significant. The important point is that "governmental action" is involved regardless of whether the milk is in-quota or over-quota.

3. Article 10.1 of the *Agreement on Agriculture*

56. New Zealand submits that Canada fails to take proper account of the purpose of Article 10.1,

61. The United States does not consider that the Panel "equated" "payments-in-kind" with "subsidies". First, the Panel focused on the circumstances of this case by referring to the "instant matter".[50] Furthermore, the Panel's finding under Article 9.1(a) is not dependent solely on the term "payments-in-kind", but was an application of the provision in its entirety. The Panel's analysis of whether the "payment-in-kind" conferred a "benefit" is part of the Panel's consideration of the subsidy issue under Article 9.1(a) as a whole.

62. Canada's argument as to the meaning of "direct" is also flawed. The term "direct" reveals nothing about either the grantor of a subsidy or the source of the funds. Indeed, Canada's own Special Import Measures Act (SIMA) Handbook relies on a very different understanding of the word "direct". It states that "a direct . . . benefit is one which accrues directly to the person, firm, or industry which is the intended recipient". This is in contrast to "an indirect benefit . . . which does not accrue directly, but which alters the economic environment within which firms operate."

63. The United States contends that Canada's argument on the first benchmark is superfluous to the appeal because the Panel relied on the second benchmark, and not the first, in making its finding. Under the second benchmark, the Panel established that there were no alternative supplies of milk, or competing products, that were available to processors on terms as favorable as those offered under

government agencies in appropriate circumstances. This interpretation is not justified by the text of Article 9.1.

68. Finally, Canada's argument on Item (d) of the Illustrative List is based entirely on the assumption that "government-mandated schemes" always involve the delegation of governmental authority. The United States does not agree with this assumption.

2. Article 9.1(c) of the *Agreement on Agriculture*

(a) "payments"

69. Contrary to Canada's arguments, the Panel did not equate "payment" with "payment-in-kind".

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73. The United States disputes Canada's suggestion that the Panel's findings under Article 9.1(c) do not stand independently from the Panel's conclusions under Article 9.1(a). Under Article 9.1(c), the Panel examined in exhaustive detail the involvement of government in the functioning and control of Special Classes 5(d) and 5(e) and Canada has not refuted the Panel's specific factual findings concerning the breadth of that involvement.

74.

79. The United States disagrees with Canada that the most relevant meaning of the word "term" is "limiting conditions", as this meaning would render the word "conditions", in the phrase "terms and conditions", entirely superfluous. It is reasonable to assume that the words "other terms and conditions" contained in Canada's Schedule are intended to mirror the language used in Article II:1(b). The similar language in this provision has been interpreted as indicating not simply additional conditions.[52] Accordingly, there is no reason for giving the entry a narrower interpretation than is justified by the ordinary meaning of its wording.

80. According to the United States, the only operative word in Canada's notation is the word "represents". However, that word gives the notation no legally operative effect. It is not the same as saying "access is limited to", or "this quantity is available only for", language which Canada could have added, as it did with respect to yoghurt and ice cream.

81. The United States agrees with the Panel's interpretation of the word "consumer".[53] The Panel was not required to spell out that "consumer" also embraces entities such as processors that "consume" milk in manufacturing. The Panel did not ignore the core issue, but found that the notation did not support the two restrictions imposed by Canada.

82. The requisite conditions for resorting to Article 32 of the *Vienna Convention* were not met and, thus, the Panel was not compelled to take into account the negotiating history. Moreover, even if Article 32 were applicable, a panel is not *required* to look to the negotiating history. That is simply "permitted". In any event, the negotiating history does not establish the existence of a common

IV. Issues Raised In This Appeal

83. This appeal raises the following issues:

(a) whether the Panel erred in its interpretation and application of Article 9.1(a) of the *Agreement on Agriculture*, in particular, with respect to:

i) the expression "direct subsidies, including payments-in-kind", and

ii) the expression "governments or their agencies";

(b) whether the Panel erred in its interpretation and application of Article 9.1(c) of the *Agreement on Agriculture*, in particular, with respect to:

i) the term "payments", and

ii) the expression "financed by virtue of governmental action";

(c) whether the Panel erred in its interpretation and application of the term "export subsidies" in Article 10.1 of the *Agreement on Agriculture*; and

(d) whether the Panel erred in finding that Canada has acted inconsistently with its obligations under Article II:1(b) of the GATT 1994 by restricting access to the tariff-rate quota for fluid milk to consumer packaged milk for personal use, valued at less than C$20, imported under the authority of General Import Permit No. 1.

V. Article 9.1(a) of the *Agreement on Agriculture*

A. "*Direct Subsidies, Including Payments-In-Kind*"

84. The Panel stated that "'payments-in-kind' are a form of direct subsidy."[54] For the Panel, it followed that "a determination in the instant matter that *'payments-in-kind'* exist *would also be* a determination of the existence of a *direct subsidy*."[55] (emphasis added) The Panel next proceeded to consider the meaning of the term "payments-in-kind". It concluded that the ordinary meaning of the word "payments", in the term "payments-in-kind", "connotes a gratuitous act, a bounty or benefit provided, for example, in pursuit of a policy objective".[56] According to the Panel, this meaning is "mandated by the general context of this provision which includes Article 1 of the

[54]Panel Report, para. 7.43.

[55]*Ibid*.

[56]*Ibid*., para. 7.44.

SCM Agreement."[57] On the basis of this interpretive framework, the Panel examined whether Special Classes 5(d) and

90. We also note that the Panel's reliance on the

B. "*Governments or their Agencies*"

93. The Panel identified the CDC, the provincial milk marketing boards and the CMSMC as playing "a direct decision-making role" in administering Special Classes 5(d) and 5(e).[68] Canada does not appeal the Panel's conclusion that the CDC, a federal Crown corporation, is an "agency" of government within the meaning of Article 9.1(a), nor does Canada specifically appeal the Panel's finding regarding the CMSMC. As regards the provincial milk marketing boards, the Panel found that they were:

> … established and operate *within a legal framework set up by federal and provincial legislation.* These boards exercise powers in respect of inter-provincial and external trade delegated to them by the federal government through the CDC, as well as powers delegated to them by provincial authorities. Three of these boards (Alberta, Nova Scotia and Saskatchewan) are, according to Canada, agencies of the provincial government. Orders or regulations issued by the provincial marketing boards can be *enforced before the Canadian courts*. In most provinces, individual decisions by the boards are subject to appeal to a provincial supervisory board or commission (of which Canada recognizes the governmental nature).[69] (emphasis added)

94. It was against this factual background that the Panel concluded that:

> It is precisely *because* the boards receive the authority from the governments to regulate certain areas themselves that their actions become governmental. What is important though is that Canadian governments maintain the ultimate control and supervision of most, if not all, of the boards' activities. These governments define, and approve changes to, the boards' mandates and functions.[70] (underlining added)

95. Since the Panel found that all of the bodies that play a decision-making role in the CMSMC are "government agencies", the Panel found that the actions of the CMSMC were the actions of a "government agency".[71]

96. Canada's appeal focuses on the Panel's findings that the provincial milk marketing boards are "government agencies". Canada takes the view that the Panel erred in law in deciding that these

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[68]Panel Report, para. 7.74.

[69]

boards are "government agencies" "*solely on the basis of one characteristic*: the delegation of some governmental authority."[72] (emphasis added)

97. We start our interpretive task with the text of Article 9.1(a) and the ordinary meaning of the word "government" itself. According to *Black's Law Dictionary*, "government" means, *inter alia*, "[t]he *regulation*, *restraint*, *supervision*, or *control* which is exercised upon the individual members of an organized jural society *by those invested with authority*".[73] (emphasis added) This is similar to meanings given in other dictionaries.[74] The essence of "government" is, therefore, that it enjoys the effective power to "regulate", "control" or "supervise" individuals, or otherwise "restrain" their conduct, through the exercise of lawful authority. This meaning is derived, in part, from the *functions* performed by a government and, in part, from the government having the *powers* and *authority* to perform those functions. A "government agency" is, in our view, an entity which exercises powers vested in it by a "government" for the purpose of performing functions of a "governmental" character, that is, to "regulate", "restrain", "supervise" or "control" the conduct of private citizens. As with any agency relationship, a "government agency" may enjoy a degree of discretion in the exercise of its functions.[75]

98. In the present case, the Panel seems to us to have applied precisely these concepts in concluding that the provincial milk marketing boards are "government agencies". Contrary to Canada's assertions, the Panel's conclusion is not based on the *sole* fact that the provincial milk marketing boards enjoy authority delegated to them by governments. To the contrary, the Panel examined both the *source* of the provincial boards' powers and the *functions* performed by those boards in the exercise of their powers. We note, furthermore, that as regards three of the provincial boards, Canada acknowledged that they were "agencies" of certain provincial governments of Canada.[76]

99. As regards the *source* of the provincial milk marketing boards' powers, it is clear that, in the words of the Panel, they "operate within a legal framework set up by federal and provincial legislation."[77] Furthermore, the provincial boards' powers and functions may only be modified by

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[72]Canada's appellant's submission, para. 116.

[73]*Black's Law Dictionary* (West Publishing Co., 1990), p. 695. The same dictionary states that "[t]he term 'jural society' is used as the synonym of 'state' or 'organized political community'" (p. 851).

[74]*The New Shorter Oxford English Dictionary*, Lesley Brown (ed.) (Clarendon Press, 1993), Vol. I, p. 1123; *Merriam Webster's Collegiate Dictionary*, Frederick Mish (ed.) (Merriam Webster Inc., 1993), p. 504.

[75]*Black's Law Dictionary*, *supra*, footnote 73, pp. 62 and 63.

[76]The boards in question are those of Alberta, Nova Scotia and Saskatchewan.

[77]Panel Report, para. 7.76.

"governments". [78] In these circumstances, it is clear, as the Panel said, that "these boards act under the

VI. Article 9.1(c) of the *Agreement on Agriculture*

A. "*Payments*"

103. In determining whether Special Classes 5(d) and 5(e) involve "payments" under Article 9.1(c), the Panel recalled that it had already found that "the provision of milk at a discdy etd

107. We have found that the word "payments", in the term "payments-in-kind" in Article

Thus, each of these three sub-paragraphs of Article 9.1 specifically contemplates that the export subsidy may be granted in a form other than a money payment.

110. The context, in our view, also includes Article 1(c) of the *Agreement on Agriculture*. In terms of that provision, "revenue foregone" is to be taken into account in determining whether "budgetary outlay" commitments, made with respect to export subsidies as listed in Article 9.1, have been exceeded. In our view, the foregoing of revenue usually does not involve a monetary payment. Thus, if a restrictive reading of the words "payments" were adopted, such that "payments" under Article 9.1(c) had to be monetary, no account could be taken, under Article 9.1(c), of "revenue foregone". This would, we believe, prevent a proper assessment of the commitments made by WTO Members under Article 9.2, as envisaged by Article 1(c) of the *Agreement on Agriculture*. We, therefore, prefer a reading of Article 9.1(c) that allows full account to be taken of "revenue foregone". The contrary view would, in our opinion, elevate form over substance and permit Members to circumvent the subsidy disciplines set forth in Article 9 of the *Agreement on Agriculture*.

111. It is true, as Canada argues, that Article 9.1(c) does not expressly include "payments-in-kind" within its scope, whereas Article 9.1(a) and paragraph 5 of Annex 2 to the *Agreement on Agriculture* do. However, we do not regard the express inclusion of "payments-in-kind" in these two provisions as necessarily implying the exclusion of "payments-in-kind" under Article 9.1(c). In Article 9.1(a) and in paragraph 5 of Annex 2, the term "payments-in-kind" is used in conjunction with the words "*direct* subsidies" and "*direct* payments", respectively. We believe that reference is made to "payments-in-kind" in these two provisions to counter any suggestion that the ordinary meaning of the terms "*direct* subsidies" and "*direct* payments" does *not* include "payments-in-kind". By contrast, since the ordinary meaning of the word "payments" in Article 9.1(c) includes "payments-in-kind", there was no need for "payments-in-kind" to be expressly provided for. Moreover, if "payments-in-kind" are *included* in the qualified concept of "direct payments" under Annex 2, paragraph 5, it would be incongruous to *exclude* them from the broader concept of "payments" in Article 9.1(c).

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the recipient is paid in the form of goods or services. But, as far as the recipient is concerned, the economic value of the transfer is precisely the same.

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117. In arguing that the Panel erred in finding that "payments" made under Special Classes 5(d) and 5(e) are "financed by virtue of governmental action", Canada maintains, first, that this finding is based on the Panel's earlier finding that the provincial milk marketing boards are "government agencies" under Article 9.1(a). Since Canada believes that the Panel's finding under Article 9.1(a) is erroneous, Canada also believes that the finding under Article 9.1(c) is flawed. Canada contends, moreover, that the "payments" are not "financed by virtue of governmental action" because the provincial milk marketing boards are composed, at least in part, of milk producers and act in the interest of those producers. Finally, Canada considers that the Panel failed to take sufficient account of important differences between the treatment of in-quota and over-quota milk, in particular, as regards the pooling of returns to producers.

118. We have rejected Canada's appeal against the Panel's finding that the provincial milk marketing boards are "government agencies". [96] Canada's first argument that the Panel's finding under Article 9.1(c) is flawed to the extent that it is based on the Panel's finding under Article 9.1(a) must, therefore, be dismissed. In our view, since all of the bodies involved in the supply of milk under Special Classes 5(d) and 5(e) are "government agencies" under Article 9.1(a), a strong presumption arises that their conduct in managing those Special Classes may appropriately be regarded as "governmental action".

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indispensable to enable the supply of milk to processors for export, and hence the transfer of resources, to take place. In the regulatory framework, "government agencies" stand so completely between the producers of the milk and the processors or the exporters that we have no doubt that the transfer of resources takes place "by virtue of governmental action".

121. We have already found, in our reasoning under Article 9.1(a), that the fact that the provincial milk marketing boards are composed, in part, of producers and act in their interests, does not alter the "governmental" character of the provincial boards' "actions".[99] Nor does the fact that, under Special Class 5(e), in-quota returns to *producers* are pooled very differently from over-quota returns alter our conclusion. The price paid for the milk by the *processors* is not, in any way, dependent on whether milk is part of in-quota or over-quota production. Moreover, even though the two pooling mechanisms differ in significant respects, they both nevertheless involve "governmental action" that remains an essential aspect of the financing of the "payments" to processors or exporters.

122. [99]

and 5(e) constitutes export subsidies, as listed in Article 9.1(c), those subsidies *cannot*, by definition, be "export subsidies *not* listed in paragraph 1 of Article 9", as required by Article 10.1. Therefore, the condition on which the Panel's alternative line of reasoning is predicated does not arise. In these circumstances, both the Panel's reasoning and its finding under Article 10.1 are completely moot and, thus, of no legal effect. There is, therefore, no reason for us to examine Canada's appeal of the Panel's finding under Article 10.1.

VIII. Article II:1(b) of the GATT 1994

125. We approach this last issue by recalling the factual background to this aspect of the dispute. The Panel stated that:

> In Part I of Canada's Schedule to GATT 1994, Canada established a tariff-rate quota for fluid milk (HS 0401.10.10 and 0401.20.10) of 64,500 tonnes. In-quota imports are subject, initially, to a maximum duty of 17.5 per cent (a rate to be decreased to 7.5 per cent in 2001). Fluid milk imports outside of the 64,500 tonnes tariff-rate quota bear an initial rate of duty equal to 283.8 per cent, declining to 241.3 per cent in 2001. In its Schedule, Canada specified under 'Other terms and conditions' that '[t]his quantity [64,500 tonnes] represents the estimated annual cross-border purchases imported by Canadian consumers'.

129. The Panel held that the meaning of the terms in Canada's Schedule could be gleaned from an examination of the "ordinary meaning [of those terms] in their context and in the light of the object and purpose of GATT 1994."[109] The Panel saw "no need to also examine the historical background against which these terms were negotiated."[110] It noted, furthermore, that the "drafting history … is inconclusive, possibly supporting both the view of Canada and that of the United States."[111] Finally, the Panel concluded that:

> … Canada, by restricting the access to the tariff-rate quota for fluid milk to (i) consumer packaged milk for personal use and (ii) entries valued at less than C$20, acts inconsistently with its obligations under Article II:1(b) of GATT 1994.[112]

130. On appeal, Canada argues, in essence, that the Panel erred by failing to ascribe any meaning, in the sense of "limiting effect", to the language in the notation in its Schedule.[113] In Canada's view, the Panel ought to have established the meaning and content of the language in the Schedule, before considering whether the specific restrictions imposed under General Import Permit No. 1 were justified by that language.

131. We explained in *European Communities – Customs Classification of Certain Computer Equipment* ("*European Communities – Computer Equipment*") that:

> A Schedule is … an integral part of the GATT 1994 …. . Therefore, the concessions provided for in that schedule are part of the terms of the treaty. As such, the only rules which may be applied in interpreting the meaning of a concession are the general rules of treaty interpretation set out in the *Vienna Convention*.[114]

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[109]Panel Report, para. 7.155.

[110]*Ibid*.

[111]*Ibid*.

[112]*Ibid*., para. 7.156.

[113]Canada's appellant's submission, para. 152.

[114]Appellate Body Report, WT/DS62/AB/R, WT/DS67/AB/R, WT/DS68/AB/R, adopted 22 June 1998, para. 84.

132. These rules call, in the first place, for the treaty interpreter to attempt to ascertain the ordinary meaning of the terms of the treaty in their context and in the light of the object and purpose of the treaty, in accordance with Article 31(1) of the *Vienna Convention*. However, as we also said in *European Communities – Computer Equipment*:

> … if after applying Article 31 the meaning of the term remains ambiguous or obscure, or leads to a result which is manifestly absurd or unreasonable, Article 32 allows a treaty interpreter to have recourse to:
>
> > ... supplementary means of interpretation, including the preparatory work of the treaty and the circumstances of its conclusion.
>
> With regard to "the circumstances of [the] conclusion" of a treaty, this permits, in appropriate cases, the examination of the historical background against which the treaty was negotiated.[115]

133. It is also well to recall that the task of the treaty interpreter is to ascertain and give effect to a legally operative meaning for the terms of the treaty. The applicable fundamental principle of *effet utile* is that a treaty interpreter is not free to adopt a meaning that would reduce parts of a treaty to redundancy or inutility.[116]

134. We start our interpretive task by noting that the language at issue in Canada's Schedule is included under the heading "Other Terms and Conditions". Under Article II:1(b) of the GATT 1994, the market access concessions granted by a Member are "*subject to*" the "terms, conditions or qualifications set forth in [its] Schedule". (emphasis added) In our view, the ordinary meaning of the phrase "subject to" is that such concessions are without prejudice to and are *subordinated to*, and are, therefore, *qualified by*, any "terms, conditions or qualifications" inscribed in a Member's Schedule. We believe that the relationship between the 64,500 tonnes tariff-rate quota and the "Other Terms and Conditions" set forth in Canada's Schedule is of this nature. The phrase "terms and conditions" is a composite one which, in its ordinary meaning, denotes the imposition of qualifying restrictions or conditions. A strong presumption arises that the language which is inscribed in a Member's Schedule

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[115] *Supra*, footnote 114, para. 86.

[116] Appellate Body Report, *United States – Standards for Reformulated and Conventional Gasoline*, WT/DS2/AB/R, adopted 20 May 1996, p. 23; Appellate Body Report, *Japan – Taxes on Alcoholic Beverages*, WT/DS8/AB/R, WT/DS10/AB/R, WT/DS11/AB/R, adopted 1 November 1996, p. 12.

under the heading, "Other Terms and Conditions", has some *qualifying* or *limiting* effect on the substantive content or scope of the concession or commitment.[117]

135. In interpreting the language in Canada's Schedule, the Panel focused on the verb "represents" and opined that, because of the use of this verb, the notation was no more than a "*description*" of the "way the size of the quota was determined".[118] The net consequence of the Panel's interpretation is a failure to give the notation in Canada's Schedule *any* legal effect as a "term and condition". If the language is

have addressed: namely, what *is* the meaning of that notation? That is, what *is* the shape and tenor of the concession that Canada had set forth in its Schedule of Commitments?

138. In our view, the language in the notation in Canada's Schedule is *not theclear or*

140. The next issue we must address is whether the measure promulgated by Canada in the form of General Import Permit No. 1 is consistent with the commitment for fluid milk in Canada's Schedule, as we read it. General Import Permit No. 1 authorizes:

> Any person … [to] *import into Canada* from any country … *any dairy products* for *the personal use* of the importer and his household *not exceeding $20 in value for each importation*. (emphasis added)

141. The first condition of General Import Permit No. 1 is that the dairy products, including fluid milk, imported into Canada must be for "the personal use of the importer and his household". This condition appears to us to be reflected in the following phrase in the notation in Canada's Schedule: "cross-border purchases imported by Canadian consumers". General Import Permit No. 1 allows, in the words of the notation, "Canadian consumers" to "import into Canada" fluid milk and other dairy products that they purchase in the United States. These are, therefore, "cross-border purchases" for the "personal use" of Canadian importers. Thus, we see the first condition of General Import Permit No. 1 as consistent with the notation at issue in Canada's Schedule.

142. The second condition of General Import Permit No. 1 is that the value of "each importation" of any "dairy products" not exceed "$20 in value". In this connection, we note that General Import Permit No. 1 applies to "dairy products" generally, not just to fluid milk. The tariff-rate quota commitment and the accompanying notation in Canada's Schedule, however, apply only to "fluid milk". Moreover, the notation at issue in Canada's Schedule does not place any limit on the value of each importation. To the extent that the second condition of General Import Permit No. 1 is not reflected in the notation at issue, the Canadian measure is not consistent with Canada's commitment on fluid milk set forth in its Schedule.

143. In light of the foregoing, we do not agree with the Panel's interpretation of the notation at issue relating to the tariff-rate quota commitment on fluid milk in Canada's Schedule. Nor do we agree with the Panel's finding that by restricting access to the tariff-rate for fluid milk to "consumer packaged milk for personal use", Canada acts inconsistently with its obligations under Article II:1(b) of the GATT 1994. However, we do agree with the Panel's finding that by restricting access to the tariff-rate quota for fluid milk to "entries valued at less than C$20", Canada acts inconsistently with its obligations under Article II:1(b) of the GATT 1994.

IX. Findings and Conclusions

144. For the reasons set out in this Report, the Appellate Body:

(a) reverses the Panel's interpretation of the terms "direct subsidies" and "payments-in-kind", as used in Article 9.1(a) of the *Agreement on Agriculture*, and, in consequence, reverses the Panel's finding that Canada, through Special Milk Classes 5(d) and 5(e), has acted inconsistently with its obligations under Article 3.3 and Article 8 of the *of ts25 Twc*

Signed in the original at Geneva this 23rd day of September 1999 by:

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Mitsuo Matsushita
Presiding Member

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Florentino Feliciano
Member

Julio Lacarte-Muró
Member