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1.1 On 20 August 1999, the Dispute Settlement Body ("DSB") adopted the Appellate Body Report in WT/DS46/AB/R, and the Panel Report in WT/DS46/R as modified by the Appellate Body Report, in the dispute (" ").

1.2 The DSB recommended that Brazil bring its export subsidies found in the Appellate Body Report, and in the Panel Report as modified by the Appellate Body report, to be inconsistent with Brazil's obligations under Articles 3.1(a) and 3.2 of the (" ") into conformity with its obligations under that Agreement. The DSB further recommended that Brazil withdraw the export subsidies for regional aircraft within 90 days.

1.3 On 19 November 1999, Brazil submitted to the Chairman of the DSB, pursuant to Article 21.6 of the Dispute Settlement Understanding ("DSU"), a status report (WT/DS46/12) on implementation of the Appellate Body's and the Panel's recommendations and rulings in the dispute. The status report described measures taken by Brazil which, in Brazil's view, implemented the DSB's recommendation to withdraw the measures within 90 days.

1.4 The status report indicated that the interest rate equalisation payments under PROEX would be granted only to the extent that the net interest rate applicable to a transaction under that programme was brought down to the appropriate international market "benchmark". The implementing legislation included: (i) a Resolution by the National Monetary Council altering its own Resolution 2576 dated 17 December 1998, which establishes the criteria applicable to PROEX interest rate equalisation payments; and (ii) a Central Bank Circular Letter which establishes new maximum equalisation percentages and revokes Circular Letter 2843 dated 25 March 1999.

1.5 On 23 November 1999, Canada submitted a communication to the Chairman of the DSB (WT/DS46/13), seeking recourse to Article 21.5 of the DSU. In that communication, Canada indicated that there was a disagreement between Canada and Brazil as to whether the measures taken by Brazil to comply with the 20 August 1999 rulings and recommendations of the DSB in fact bring Brazil into conformity with the provisions of the and result in the withdrawal of the export subsidies to regional aircraft under PROEX and Canada, therefore, requested that the DSB refer the matter to the original panel, pursuant to Article 21.5 of the DSU. Canada attached the terms of an agreement reached by Canada and Brazil concerning the procedures to be followed pursuant to Articles 21 and 22 of the DSU.

1.6 At its meeting on 9 December 1999, the DSB decided, in accordance with Article 21.5 of the DSU, to refer to the original panel the matter raised by Canada in document WT/DS46/13. At that DSB meeting, it also was agreed that the Panel should have standard terms of reference as follows:

> "To examine, in the light of the relevant provisions of the covered agreements cited by Canada in document WT/DS46/13, the matter referred to the DSB by Canada in that document and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements."

1.7 The Panel was composed as follows:

Chairperson: Dr. Dariusz Rosati

Members: Prof. Akio Shimizu

Mr. Kajit Sukhum

1.8 Australia, the European Communities and the United States reserved their rights to participate in the Panel proceedings as third parties.

1.9 The Panel met with the parties on 3-4 February 2000. It met with the third parties on 4 February 2000.

1.10 The Panel submitted its interim report to the parties on 31 March 2000. On 7 April 2000, Brazil submitted a written request that the Panel review precise aspects of the interim report. Neither party requested an interim meeting. The Panel submitted its final report to the parties on 28 April 2000.

2.1 As described in our original Panel Report,[1]

2.5 PROEX involvement in aircraft financing transactions begins when the manufacturer requests a letter of commitment 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 the Government of Brazil 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 (and provided the aircraft is exported, as explained below). If a contract is not entered into within the specified time, the commitment contained in the letter of approval expires.

2.6 PROEX interest rate equalisation 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 ( ), referred to as NTN-I bonds. 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-month 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.

3.1 requests that the Panel find that Brazil's measures are not in compliance with the recommendations and rulings of the DSB in that, , Brazil continues to pay export subsidies committed on exports of regional aircraft not yet granted as of 18 November 1999; and, , Brazil has failed to implement measures that would bring the PROEX export subsidy programme into conformity with the , because: (a) PROEX payments continue to constitute prohibited export subsidies, (b) the first paragraph of item (k) of the Illustrative List of Export Subsidies, Annex I, ("Illustrative List"), does not give rise to an exception, and (c) even if item (k) were considered to give rise to an exception, PROEX export subsidies are not "payments" of the kind referred to in the first paragraph of item (k) and PROEX export subsidies under the revised programme would continue to "secure a material advantage" in the field of export credit terms. Canada further requests that the Panel suggest, in accordance with Article 19.1 of the DSU, that the parties develop verification procedures so as to permit verification that future Brazilian financing of exported regional aircraft conforms with the without the need for further recourse to the DSU.

3.2 requests the Panel to reject Canada’s claims in their entirety, and find that Brazil is in full compliance with all of its obligations under the , as interpreted by the Panel and the Appellate Body, with regard to PROEX interest rate equalisation payments for regional aircraft.

4.1 The Panel has decided, with the agreement of the parties, that in lieu of the Treted Tc 1S1e3pv0

establish that an export subsidy is "permitted" and whether payments under PROEX are "payments" within the meaning of the first paragraph of item (k) of the List.[7]

5.1 Canada did not provide any comments on the interim report of the Panel.

5.2 Brazil submitted the following comments. Brazil notes that, in paragraph 6.41, , the Panel states that it does not appear that Brazil argued that its interpretation of paragraph 1 of item (k) of the Illustrative List applied even when the subsidies "do not fall within the scope of footnote 5". Brazil states that it does not recall confining its interpretation of item (k) to the "scope of footnote 5", and certainly did not intend to do so. In this regard, Brazil notes that, in response to a question from the Panel, Brazil stated, "Footnote 5 to the SCM Agreement makes clear that the List has a purpose other than pure illustration."[8] Beyond this, Brazil submits, the response deals with the text of item (k), not the scope of footnote 5.

5.3 With reference to Brazil's argument that its interpretation of item (k) was not confined to the scope of footnote 5, we note that, in the original dispute, Brazil's arguments appeared to evolve over time.[9] In Brazil's first submission in the original dispute, the focus of Brazil's arguments was not on footnote 5.[10] However, in its second submission in the original dispute, Brazil argued that the "material advantage" clause fell within the scope of footnote 5.[11] Brazil has not, however, limited its arguments regarding the interpretation of item (k) to the scope of footnote 5, and we have, therefore, made appropriate modifications to paragraph 6.41 of this Report. In any event, as we have indicated in paragraph 6.41, we consider that footnote 5 controls the interpretation of item (k) with respect to when the Illustrative List can be used to demonstrate that a measure is not a prohibited export subsidy.

5.4 Brazil also notes that, in paragraph 6.53 of this Report, the third sentence begins, "Because ____ in many cases have a lower cost of borrowing than the governments of developing countries . . ." (Emphasis added by Brazil). Brazil argues that, if banks were the only actors in the market for aircraft financing, Brazil would not need to provide interest rate support for Embraer's transactions. It is the fact that (Emphasis added by Brazil) – particularly Canada through its Export Development Corporation – are able to offer potential customers financing support on terms that are more attractive than the terms offered by banks that requires Brazil to act.

5.5 In respect of Brazil's comments regarding the Panel's reference to the cost of borrowing of banks, the Panel wishes to point out that paragraph 6.53 of this Report represents a discussion of the way in which developing-country governments can utilise commercial lenders rather than provide direct export credit financing. The Panel in fact paraphrases Brazil's own arguments as to the relative cost of different modalities of providing export credits.[12] In that context, it is clear that utilising commercial lenders would be less expensive than providing direct financing, because the government can take advantage of the lower cost of borrowing enjoyed by commercial lenders. Footnote 53 is merely an illustration of this fact. Paragraph 6.53 is in no sense intended to suggest that Brazil argues that it provides PROEX interest rate equalisation in order to meet competition from export credit financing provided by commercial banks. We have, therefore, made appropriate modifications to paragraph 6.53 of this Report.

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[7] Original Panel Report, paras. 4.53-4.71 and paras. 4.72-4.78, respectively.

[8] Response of Brazil to Question 10 from the Panel, , Annex 2-4, p. 133.

[9] As indicated in para. 4.2, , Brazil has incorporated by reference its arguments in the original dispute regarding whether the first paragraph of item (k) of the Illustrative List may be used to establish that an export subsidy is "permitted". Response of Brazil to Further Question 1 from the Panel, , Annex 2-4, p. 137.

[10] original Panel Report, paras. 4.53-4.54.

[11] , at para. 4.67.

[12] Oral Statement of Brazil, paras. 11-20, , Annex 2-3, p. 115.

A. INTRODUCTION AND CLAIMS OF CANADA

6.1 This dispute under Article 21.5 of the DSU concerns a disagreement between Canada and Brazil as to the existence or consistency of measures taken by Brazil to comply with the recommendation of the DSB pursuant to Article 4.7 of the that Brazil withdraw export subsidies for regional aircraft under PROEX without delay. [13]

6.2 In the dispute ("original dispute") giving rise to this Article 21.5 dispute, the Panel found that the prohibition on export subsidies in Article 3.1(a) of the applied to Brazil because Brazil had failed to comply with certain of the conditions of Article 27.4 of that Agreement. The Panel further found that PROEX payments were subsidies contingent upon export performance within the meaning of Article 3.1(a). Finally, the Panel rejected Brazil's defence that PROEX payments were "permitted" because they were "payments" within the meaning of the first paragraph of item (k) which were not "used to secure a material advantage in the field of export credit terms". The Panel found that, that the first paragraph of item (k) could be used to establish that a subsidy that is contingent upon export performance was "permitted", and that PROEX payments were "payments" within the meaning of that paragraph, Brazil had failed to establish that PROEX payments were not "used to secure a material advantage in the field of export credit terms". Accordingly, the Panel requested that the DSB recommend that Brazil withdraw the prohibited subsidies without delay. The Appellate Body modified certain aspects of the Panel's reasoning but upheld the Panel's conclusions as stated above.

6.3 In this Article 21.5 dispute, Canada raises two issues regarding the existence or consistency with the of measures taken by Brazil to comply with the recommendation of the DSB.

> , Canada contends that Brazil cannot, consistent with the recommendation of the DSB, continue to issue NTN-I bonds pursuant to letters of commitment issued under PROEX as it existed prior to the end of the implementation period, , 18 November 1999. Brazil responds that the DSB's recommendation to withdraw the prohibited subsidy does not require it to cease issuing NTN-I bonds pursuant to such pre-existing letters of commitment.
>
> , Canada contends that payments in respect of regional aircraft pursuant to PROEX as modified by Brazil continue to be subsidies contingent upon export performance within the meaning of Article 3.1(a) of the and thus prohibited. Brazil responds that under PROEX as modified payments no longer are "used to secure a material advantage in the field of export credit terms" and therefore are "permitted" by the .

We will take up each of these issues in turn.

B. MAY 98 TD /F3 11.*70.0013 T B7se issuing NTN-I bonds pursuant to such pre-exist7NUE TO ISSUE Tj 0 -BONDS PURSUANT TO LETTERS OFt terms" and therefore011 11.25 1 In4this Article21.5 dispute, Canada raises tw1192.75 TD8640 TD / 3.2674 laimw (DSB, continhntafail604

18 November 1999, the date by which Brazil was required to withdraw the export subsidies in question. Brazil considers that, in fulfilling its pre-18 November 1999 commitments through the issuance of NTN-I bonds after that date upon the export of regional aircraft, it is "not creating new subsidies"[14] and therefore not acting in a manner inconsistent with its obligations under the .

6.5 Canada notes that Brazil is required to withdraw the prohibited export subsidies, and submits that the word "withdraw", in its plain meaning, conveys as a minimum the notion of ceasing to grant or maintain the illegal subsidies. Article 3.2 of the provides that a Member shall not "grant or maintain" prohibited subsidies. Canada recalls that the Appellate Body had found that PROEX subsidies are granted for the purposes of Article 27.4 of the when Brazil issues NTN-I bonds. There is no reason in Canada's view to interpret the word "grant" differently for the purposes of Article 3.2 than for the purposes of Article 27.4. Accordingly, Brazil must, in Canada's view, cease issuing NTN-I bonds in respect of pre-18-November-1999 letters of commitment.

6.6 In Brazil's view, Canada has confused the finding of the Appellate Body as to when PROEX subsidies are granted for the purposes of Article 27.4 of the with the issue of when PROEX subsidies come into existence within the meaning of Article 1 of that Agreement. Brazil considers that under Article 1 a subsidy shall be deemed to exist when there is a financial contribution by a government and a benefit is thereby conferred. In the case of PROEX subsidies, the benefit arises when Brazil makes a legally binding commitment to provide PROEX support.[15] Because the financial contribution must logically precede or coincide with the benefit, the financial contribution must be in the form of a potential direct transfer of funds. In the view of Brazil, an interpretation of Article 1 that resulted in the conclusion that PROEX subsidies come into existence only when aircraft are exported would render whole clauses of Part III of the ("Actionable Subsidies") a nullity because, although the impact of PROEX on the domestic industry of a competitor would be felt when Embraer obtains an order, no subsidy would exist and thus no countervailing measure be possible until the aircraft was exported. Finally, Brazil argues that it is legally obligated to issue bonds pursuant to letters of commitment issued prior to the date of implementation of the DSB's recommendations or be subject to damages for breach of contract.

6.7 In considering this issue, we first note that Brazil does not deny that it continues to issue NTN-I bonds in respect of commitments made prior to 18 November 1999. Further, Brazil has stated, in response to a question from the Panel, that Resolution 2667 does not modify pre-existing PROEX commitments pertaining to aircraft to be exported after 22 November 1999, the date of publication of Resolution 2667.[16] We recall that, in the original dispute, the Panel found that PROEX payments on exports of Brazilian regional aircraft were export subsidies prohibited by Article 3.1(a) of the . This finding was upheld by the Appellate Body. We also recall that the DSB

have withdrawn prohibited subsidies if it has not ceased to act in a manner inconsistent with the in respect of those subsidies. We are therefore of the view that the DSB's recommendation that Brazil withdraw the prohibited subsidies in question clearly includes an obligation on the part of Brazil to cease violating the by the end of the implementation period in respect of the measures in question.[17]

6.9 Article 3.2 of the provides as follows:

> "A Member shall neither grant nor maintain subsidies [contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I]."

It follows that the continuing granting or maintaining of prohibited export subsidies after the end of the implementation period would be inconsistent with Brazil's obligation to withdraw those subsidies. Accordingly, we must consider whether the continued issuance of NTN-I bonds by Brazil pursuant to letters of commitment issued under PROEX prior to its modification constitutes the "grant" of prohibited export subsidies within the meaning of Article 3.2 of the .

6.10 In the original dispute, we held that, for the purposes of Article 27.4, export subsidies for regional aircraft under PROEX are "granted" for the purposes of calculating the level of Brazil's export subsidies under Article 27.4 of the when the NTN-I bonds are issued. Brazil appealed this finding. The Appellate Body confirmed our holding, finding that:

> "We agree with the Panel that '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.' We also agree with the Panel that the export subsidies . . . have not yet been 'granted' when the letter of commitment is issued, because, at that point, the export sales contract has not yet been concluded and the export shipments have not yet occurred. For the purposes of Article 27.4, we conclude that the export subsidies . . . are 'granted' when all the legal conditions have been fulfilled that entitle the beneficiary to receive the subsidies. We share the Panel's view that such an unconditional legal right exists when the NTN-I bonds are issued."[18]

6.11 We note that Article 3.2 and Article 27.4 are provisions of the same Agreement. Further, both provisions relate to the prohibition on export subsidies set out under that Agreement. We do not perceive any basis to attribute to the term "grant" as used in Article 3.2 of the a

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[17] We are aware that a panel established under Article 21.5 of the recently found that a recommendation to "withdraw" a prohibited subsidy under Article 4.7 of the "is not limited to prospective action only but may encompass repayment of the prohibited subsidy." , Recourse to Article 21.5 of the by the United States, Report of the Panel adopted on 11 February 2000, WT/DS126/RW, para. 6.39. In that dispute, which involved one-time subsidies paid in the past whose retention was not contingent upon future export performance, the United States as complainant argued that the "prospective portion" of the subsidy granted by Australia, , $A26 million out of a total grant of $A30 million, had to be repaid. In this dispute, Canada has not claimed that the non-repayment, in whole or in part, of subsidies granted by Brazil represents a failure to "withdraw" the prohibited export subsidies in question. We recall that, under Article 3.7 of the , the aim of the dispute settlement mechanism is to secure a positive resolution to a dispute, and that our role under Article 21.5 is to render a decision "where there is disagreement" as to the existence or consistency with a covered agreement of measures taken to comply with the recommendations or rulings of the DSB. Accordingly, we shall address only claimsubsidy lmhdraw" a prohal behe 1.6cOD

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meaning different from that attributed to that term by this Panel and the Appellate Body as used in Article 27.4 of the . It follows that the issuance of NTN-I bonds by Brazil constitutes the granting of export subsidies within the meaning of Article 3.2.

6.12 Brazil urges the Panel to consider the issue of when a subsidy may be deemed to exist under Article 1 of the , and the form of the financial contribution involved, when deciding when PROEX subsidies are granted for the purposes of Article 3.2. Thus, Brazil states, in response to a question from the Panel, that:

> ". . . a financial contribution is made and a benefit is conferred within the meaning of Article 1 of the , , when contracts are signed pursuant to letters of commitment." (emphasis added)

6.13 We recall however that the Panel, in order to respond to the question of when PROEX payments should be considered to have been granted for the purposes of Article 27.4 in the original dispute, also focused on the language of Article 1 of the . The Appellate Body held, however, held this to be error:

> "In our view, the Panel reached the correct conclusion. However, it did so on the basis of faulty reasoning. The issue in this case is when the subsidies for regional aircraft under PROEX should be considered to have been "granted" . The issue is whether or when there is a "financial contribution", or whether and when the subsidy "exists", within the meaning of Article 1.1 of that Agreement."(emphasis in original.)[19]

The Appellate Body further explained that:

> "[T]he issue before the Panel under the heading 'Has Brazil increased the level of its export subsidies?' was simply this: given that the export subsidies in this case were already deemed to 'exist', when were they 'granted'? At issue was the interpretation and application of Article 27.4, of Article 1 . . . [F]or the purposes of Article 27.4, we see the issue of the of a subsidy and the issue of the point at which that subsidy is as two legally distinct issues (emphasis in original). Only one of those issues is raised here and, therefore, must be addressed".[20]

6.14 We recognize that the distinction made by the Appellate Body was between the existence of a subsidy and when a subsidy is granted related to when a subsidy is granted of the , and not when it was granted . As a matter of logic, however, we cannot perceive – nor has Brazil identified – any basis for us to conclude that, while the existence of a subsidy is a legally distinct issue from when it is granted for the purposes of Article 27.4, it is a legally distinct issue from when it is granted for the purposes of Article 3.2. In other words, if the issue of when a subsidy is "granted" is legally distinct from when it "exists" for the purposes of Article 1, then it follows that the issue of when a subsidy is granted is also legally distinct from the issue when it is exists for the purposes of Article 1. Accordingly, we decline Brazil's invitation to consider when

[19] Appellate Body Report, para. 154.
[20] Appellate Body Report, para. 156.

the subsidy "exists" within the meaning of Article 1 when examining when the subsidy is "granted" for the purpose of Article 3.2.[21]

6.15 Brazil contends that requiring Brazil to cease issuing NTN-I bonds pursuant to commitments made prior to 18 November 1999 amounts to a retroactive remedy. We cannot agree. In our view, the obligation to cease performing illegal acts in the future is a fundamentally prospective remedy.[22]

6.16 Nor are we convinced that a different interpretation is required because Brazil asserts that it has a contractual obligation to issue PROEX bonds pursuant to commitments already entered into, and that it would be liable to damages for breach of contract if it failed to do so. Assuming that Brazil is correct in this regard,[23] the implication of this view would be that Members could contract to grant prohibited subsidies for years into the future and be insulated from any meaningful remedy under the WTO dispute settlement system. Nor is this a purely hypothetical situation. If Canada's figures are correct – and Brazil has not disputed their overall accuracy – Brazil has outstanding commitments to issue NTN-I bonds pursuant to PROEX as it existed before modification in respect of nearly 900 regional aircraft that have yet to be exported. Letters of commitment in respect of some 300 regional aircraft were issued after the Panel Report in the original dispute was circulated to Members on 14 April 1999. By Brazil's reasoning, it should be allowed to continue issuing bonds upon the exportation of these aircraft for years to come.

6.17 For all of the reasons set forth above, we conclude that the continued issuance of NTN-I bonds pursuant to letters of commitment issued prior to 18 November 1999 represents the granting of subsidies contingent upon export performance within the meaning of Article 3.2 of the SCM. Accordingly, we conclude that in this respect Brazil has failed to implement the recommendation of the DSB that it withdraw the export subsidies for regional aircraft under PROEX within 90 days.

recommendation of the DSB in respect of payments on exports of regional aircraft pursuant to letters of commitment issued under PROEX after its modification by Brazil.

6.22

> upon export performance within the meaning of Article 3.1(a) of that Agreement. The Panel did not rule on these issues, and the lack of Panel findings on these issues was not appealed."[30]

6.27 Nor do we accept Brazil's contention that we should infer some implicit finding on this issue by the Appellate Body. The fact that the Appellate Body considered and decided the issue of whether PROEX payments are used to "secure a material advantage in the field of export credit terms" does not mean that the Appellate Body accepted (nor, for that matter, that it rejected) Brazil's view that the first paragraph of item (k) can be used to establish that an export subsidy is "permitted". We decline to speculate about how the Appellate Body might have resolved this issue had it been before it. Rather, we will make our finding on this issue on the basis of the as interpreted in accordance with customary rules of public international law.

6.28 In examining whether the first paragraph of item (k) can be used to establish that a subsidy which is contingent upon export performance within the meaning of Article 3.1(a) is nevertheless "permitted", our starting point is of course the text of the . In this respect, and turning first to the text of Article 3.1(a), we note that that Article states that:

> "Except as provided in the Agreement on Agriculture, the following subsidies within the meaning of Article 1, shall be prohibited:
>
> (a) Subsidies contingent [footnote omitted], in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I[5];
>
> ……………………………………………………………………………………….
>
> [5] Measures referred to in Annex I as not constituting export subsidies shall not be prohibited under this or any other provision of this Agreement.

6.29 Leaving aside for the moment the issue of the role of footnote 5 – an issue to which we will return shortly – we consider that two conclusions can be derived from the text of Article 3.1(a).

6.30 , Annex I is purely illustrative, , it does not purport to be an exhaustive list of export subsidies. In other words, it contains examples of prohibited export subsidies. It is clear, however, that it is legally possible – and, as a matter of fact, highly likely – that there are prohibited export

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6.32 There is however a third conclusion that we cannot draw from the text of Article 3.1(a). Canada argues that a finding that the Illustrative List could be used to establish that measures were "permitted", would turn the Illustrative List into an exhaustive list. We do not agree. Rather, another possible interpretation is that offered by Brazil but perhaps expressed most clearly by the United States as third party:

> "The Illustrative List does not deal with all possible financial contributions, but for those it does deal with, it establishes, by virtue of footnote 5, a dispositive legal standard insofar as prohibited subsidies are concerned."[31]

Without necessarily agreeing with the US interpretation of the role of the Illustrative List – as our subsequent discussion will clearly demonstrate – we do not consider that we can conclude, based on the mere fact that the Illustrative List is "illustrative", that the List cannot be used .

6.33 How thus may we resolve the question whether and under what conditions the Illustrative List can be used to demonstrate that a subsidy which is contingent upon export performance is prohibited, , that it is "permitted"? One possibility would be to resort to general interpretive techniques. Thus, it could be argued that the Panel should interpret the Illustrative List , a term defined as meaning "on the other hand; in the opposite sense",[32] or should apply the principle of . For the reasons discussed below, however, we need not rely on such general principles in this case.

6.34 The drafters of the must have recognized that the insertion of the Illustrative List of Export Subsidies – which was imported with only minor modifications from the Tokyo Round – into an Agreement that contained for the first time definitions of "subsidy" and "export subsidy" would create interpretive difficulties, as the provides us with a specific textual basis to resolve this question. This textual basis is footnote 5 to the

6.40 We agree with the United States that the deletion of the term "expressly" appears to have broadened the scope of footnote 5 in beyond its scope in . We do not agree, however, that it served to broaden footnote 5 to the extent suggested by the United States. As we discussed above, the Illustrative List contains – and already contained at the time of and – a number of provisions that include affirmative statements that arguably represent authorizations to use certain measures. The language of

6.47 We agree with Brazil that the

"gentlemen's" agreement, negotiated in the context of the Organization for Economic Cooperation and Development. The purpose of the , as stated in its Introduction, is to "provide a framework for the orderly use of officially supported export credits" and to "encourage competition among exporters from the OECD-exporting countries based on quality and price of goods and services rather than on the most favourable officially supported terms". The sets forth certain guidelines with respect to the terms and conditions of officially supported export credits with repayment terms of two years or more, including minimum interest rates for export credits benefiting from official financing support[52] based on Commercial Interest Reference Rates, or CIRRs. There is a CIRR for the currency of each Participant to the , which is constructed based upon long-term bond yields for that Participant plus a fixed margin (which for most currencies is 100 basis points, , one percentage point).

6.52 Brazil does not dispute that any Member, whether or not a Participant to the , can invoke the second paragraph of item (k) in respect of its export credit practices which are in conformity with interest rate provisions of the . Thus, in the case at hand, Brazil could provide dollar-denominated export credits in respect of Brazilian regional aircraft on terms that might otherwise be prohibited by Article 3.1(a) of the , provided those export credits conformed to the interest rate provisions of the .

6.53 Brazil argued, however, that developing countries could not afford to provide direct export credit financing at the CIRR rate, because of their high cost of funds, and thus could not in practice use the safe harbour created by the second paragraph of item (k). In order to avoid the high cost of direct financing, developing countries such as Brazil had to use a system of payments in support of export credits provided through commercial banks. Because commercial lenders in many cases have a lower cost of borrowing than the governments of developing countries, those governments could afford to "buy down" interest rates provided by commercial lenders at much lower cost than if they offered direct export credit financing itself.[53] Thus, developing countries needed to be able to use the first paragraph of item (k) as a safe harbour for payments that were equivalent in effect to the direct financing provided pursuant to the safe harbour in the second paragraph of item (k) by developed countries. This would only be possible if the first paragraph of item (k) could be used to establish that "payments" under the first paragraph of item (k) were "permitted" under certain circumstances.

6.54 Brazil's argument in the original dispute was not well-founded. Under the , minimum interest rates in the form of CIRRs apply with respect to "official financing support", which includes "interest rate support". Thus, there is no reason why a developing country could not invoke the second paragraph of item (k) in respect of a payment scheme such as PROEX, provided that it is "in conformity with the interest rate provisions" of the . In short, Brazil's argument that developing country Members needed to be able to use the first paragraph of item (k) as a safe harbour for their export credit interest buy-down schemes (and that footnote 5 thus had to be interpreted to

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Understandings" (relating to ships, nuclear power plants, and civil aircraft) are annexed to the , and that for some products – not including regional aircraft – a minimum interest rate different from the CIRR applies. We assume – but need not here decide – that an export credit practice in conformity with the interest rate provisions of these Sector Understandings would also be entitled to the safe harbour of the second paragraph of item (k).

[52] As discussed at footnote 68, "official support" is a broader concept than "official financing support".

[53] To take a hypothetical and highly simplified example, imagine that the yield on the relevant US Government bonds (and thus the US Government's cost of borrowing) is 5 per cent, Brazil's cost of borrowing is

apply in respect of the first paragraph of item (k)) because they could not in practice benefit from the safe harbour in the second paragraph was, in our view, simply incorrect.[54]

6.55 In this implementation dispute, Brazil continues to argue that it must be allowed to use the first paragraph of item (k) to establish that an admitted export subsidy is "permitted" so that it can ensure the availability of WTO-consistent export credit financing for Brazilian products on terms equivalent to those that Canada is allowed to provide by the and the . Specifically, Brazil 0 -11,that Canada is allowed ty the

. As noted earlier in this Report (para. 6.52,), the export credit practice of a Member which is not a Participant to the but which "in practice applies the interest rate provisions" of the benefits from the safe harbour of the second paragraph of item (k) provided that the practice is "in conformity with those [, the interest-rate] provisions."

6.62 We have already seen that, even if a developing country Member cannot in practice afford to

interest rate under the is the CIRR. Thus, an export credit which is provided through "market windows" at an interest rate below CIRR cannot be said to be "in conformity with" the interest rate provisions of the and thus cannot benefit from the safe harbour provided for in that paragraph.[68] Accordingly – and in light of our understanding of the ordinary meaning of

export credit terms because such findings should facilitate Brazil's task in implementing the DSB's recommendations.

6.69 Brazil argues that PROEX payments constitute the payment by Brazil of all or part of the costs incurred by Embraer or financial institutions in obtaining credits within the meaning of the first paragraph of item (k). As explained in our original Panel Report,[71] Brazil's argument appears to be two-fold. Brazil contends that financial institutions must borrow funds in order to finance their lending, that the export credits so funded are provided at below their cost of borrowing, and that PROEX payments are provided to compensate the lenders for this difference. The difference between the lender's cost of borrowing and the rate it charges on the export credits represents a "cost incurred by . . . financial institutions in obtaining credits". , Brazil asserts that, although Embraer does not itself extend export credits to its customers, it incurs certain costs in relation to the provision of export credits by financial institutions. Brazil's arguments are linked to the principle that both Embraer and Brazilian financial institutions have high costs of borrowing as a result of "Brazil risk", , the Government of Brazil has a high cost of borrowing and Brazilian entities cannot borrow on terms more favourable than those of their government.

6.70 Canada agrees with the basic thrust of Brazil's interpretation of the notion of payments. In Canada's view, a payment exists within the meaning of the first paragraph of item (k) where an exporter or financial institution obtains credits at an interest rate higher than the rate at which it would provide export credits to a buyer and incurs a cost as a result, and the government pays for all or part of this difference. In Canada's view, however, PROEX payments are not "payments" in this sense. In

export credits. In this respect, we note that Brazil's argument focused on the fact that Embraer and Brazilian financial institutions had a high cost of borrowing as a result of "Brazil risk". As Canada points out, however, Embraer does not itself provide export credit financing, and the financial institutions receiving PROEX payments are not necessarily Brazilian financial institutions. Rather, they are in many cases leading international financial institutions unhampered by "Brazil risk". Thus, there is no basis for us to conclude, nor even to hypothesise, that the financial institutions in question are providing export credits at below their cost of funds.

6.74 The third and final element of Brazil's material advantage defence is that PROEX payments are not "used to secure a material advantage in the field of export credit terms" within the meaning of the first paragraph of item (k).

6.75 Brazil considers that it has modified PROEX in respect of regional aircraft such that PROEX payments are no longer used to secure a material advantage in the field of export credit terms. Specifically, Brazil argues that Resolution 2667

> "means, effectively . . . that no application for PROEX interest rate equalisation support for regional aircraft will be favorably considered unless it reflects a net interest rate to the borrower equal to or more than the 10-year United States Treasury Bond ('T-Bill') plus 0.2 percent per annum. While the use of the T-Bill as the benchmark is preferred, the authorities retain the authority to utilise LIBOR as an alternative reference point in appropriate market circumstances "[72]

Brazil requests the Panel to find that, "by requiring the net interest rate for any transaction supported by PROEX to equal or exceed an appropriate market benchmark – with the preferred benchmark being the T-Bill plus 20 basis points – Brazil has withdrawn the prohibited aspects of the PROEX programme."[73]

6.76 In order to determine whether Brazil is correct in its view that payments pursuant to the PROEX scheme no longer are used to secure a material advantage in the field of export credit terms, we must first seek to resolve certain differences of view among the parties regarding the meaning of the "material advantage" clause as interpreted by the Appellate Body, and in particular the role of the CIRR in determining whether payments are or are not used to secure a material advantage in the field of export credit terms.

6.77 In Brazil's view, the Appellate Body found that PROEX was flawed because it lacked a benchmark based on the marketplace. According to Brazil, the Appellate Body found that Members are permitted to obtain an "advantage" in the field of export credit terms provided that advantage is not "material". It also made clear that the appropriate benchmark for determining whether a material advantage is secured is the marketplace and not a specific transaction.[74] Put another way, Brazil argues that the "primary flaw" in PROEX identified by the Appellate Body was "the absence of a floor net interest rate based on a cognizable benchmark rate in the commercial marketplace."[75] In the view of Brazil, while the Appellate Body identified the CIRR as 'one example' of an appropriate

[72] First Submission of Brazil, para. 6.
[73] Second Submission of Brazil, para. 40.
[74] First Submission of Brazil, para. 4.
[75] Second Submission of Brazil, para. 30.

benchmark, Brazil chose a point of reference other than CIRR for PROEX based on evidence that, in the case of aircraft, the marketplace in fact supports lower interest rates .[76]

6.78 Canada sees no basis in the rulings of the Appellate Body for Brazil's claim to a benchmark below CIRR even if Brazil could demonstrate that interest rates in the marketplace were below CIRR at some given moment. In the view of Canada, the Appellate Body used the second paragraph of item (k), and therefore the , as useful context for arriving at the appropriate benchmark to be used in the first paragraph of item (k). The Appellate Body found that the CIRR constituted the commercial interest rate for the purposes of the . It determined accordingly that a net interest rate below the relevant CIRR was a positive indication that material advantage was being secured. There was no suggestion at all by the Appellate Body that any other, lower benchmark could appropriately be used instead of CIRR for item (k).

6.79 From the above, it is evident that Canada and Brazil have fundamentally different views about the legal significance of the CIRR as a benchmark for determining whether or not a payment is used to secure a material advantage. Canada considers that a payment that results in a net interest rate below CIRR secures a material advantage. Brazil considers that a lower benchmark for determining whether a payment is used to secure a material advantage would be appropriate if it could be established that the "marketplace" in fact supports lower rates.

6.80 As noted above, Resolution 2667 sets what Brazil characterises as a minimum net interest rate for export credits supported by PROEX payments based on US 10-year Treasury Bonds plus 0.2 per cent (20 "basis points"). Canada argues, and Brazil does not dispute, that such a minimum interest rate is below CIRR.[77] Accordingly, if Canada is correct in its view that a payment that results in a net interest rate below the CIRR is used to secure a material advantage, then PROEX payments are used to secure a material advantage. On the other hand, if Brazil is correct that an interest rate below CIRR does not imply a material advantage if the marketplace supports such a lower interest rate, then we must examine the evidence submitted by the parties in respect of the interest rates in the marketplace for regional aircraft.

6.81 In considering this issue, we have carefully reviewed the Report of the Appellate Body in the original dispute. The Appellate Body had before it the conclusion of the Panel that a 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 in the marketplace with respect to the transaction in question".[78] The Appellate Body rejected the Panel's interpretation for two reasons. First, the Appellate Body found that the Panel had omitted the term "material" from its test, thus reading that term out of item (k). Second, the Appellate Body found that the Panel had interpreted the material advantage clause as equivalent to the term "benefit" in Article 1.1(b) of the , thereby rendering that clause meaningless.

6.82 The Appellate Body then explained how the "material advantage" clause should properly be

180. We note that there are two paragraphs in item (k), and that the "material advantage" clause appears in the first paragraph. Furthermore, the second paragraph is a proviso to the first paragraph. The second paragraph applies when a Member is "a party to an international undertaking on official export credits" which satisfies the conditions of the proviso, or when a Member "applies the interest rates provisions of the relevant undertaking". In such circumstances, an "export credit practice" which is in conformity with the provisions of "an international undertaking on official export credits" shall not be considered an export subsidy prohibited by the . The is an "international undertaking on official export credits" that satisfies the requirements of the proviso in the second paragraph in item (k). However, Brazil did not invoke the proviso in the second paragraph of item (k) in its defence. Brazil argued before the Panel that it "has concluded that conformity to the OECD provisions is too expensive."[footnote omitted].

181. Thus, this case falls under the first paragraph, and not under the proviso of the second paragraph, of item (k) of the Illustrative List. Consequently, the issue here is whether the export subsidies for regional aircraft under PROEX "are used to secure" for Brazil "a material advantage in the field of export credit terms". Nevertheless, we see the second paragraph of item (k) as useful context for interpreting the "material advantage" clause in the text of the first paragraph. The establishes minimum interest rate guidelines for export credits supported by its participants ("officially-supported export credits"). Article 15 of the defines the minimum interest rates applicable to officially-supported export credits as the Commercial Interest Reference Rates ("CIRRs"). Article 16 provides a methodology by which a CIRR, for the currency of each participant, may be determined for this purpose. We believe that the can be appropriately viewed as one example of an international undertaking providing a specific market benchmark by which to assess whether payments by governments, coming within the provisions of item (k), are "used to secure a material advantage in the field of export credit terms". Therefore, in our view, the appropriate comparison to be made in determining whether a payment is "used to secure a material advantage", within the meaning of item (k), is between the actual interest rate applicable in a particular export sales transaction after deduction of the government payment (the " interest rate") and the relevant CIRR.

182. It should be noted that the commercial interest rate with respect to a loan in any given currency varies according to the length of maturity as well as the creditworthiness of the borrower. Thus, a potential borrower is not faced with a single commercial interest rate, but rather with a range of rates. Under the , a CIRR is the commercial rate available in that range for a particular currency. In any given case, whether or not a government payment is used cting the 31ecific market benchmar0.3191 4.0367(minimuml) Tj 0 -12.38 TD /F1 11.25 Tf -0.1479 Tc 5.87

> Panel.[footnote omitted]. Because Brazil provided on the net interest rates paid by purchasers of Embraer aircraft in actual export sales transactions, we have no basis on which to compare the net interest rates resulting from the interest rate equalisation payments made under PROEX with the relevant CIRR.
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> 184. Accordingly, we find that Brazil has failed to meet its burden of proving that export subsidies for regional aircraft under PROEX are not "used to secure a material advantage in the field of export credit terms" within the meaning of item (k) of the Illustrative List.
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> 185. We are aware that the allows a government to "match", under certain conditions, officially-supported export credit terms provided by another government. In a particular case, this could result in net interest rates below the relevant CIRR. We are persuaded that "matching" in the sense of the is not applicable in this case. Before the Panel, Brazil argued for an interpretation of the clause "in the field of export credit terms" that would include as an "export credit term" the price at which a product is sold, and maintained that, therefore, Brazil was entitled to "offset" provided to Bombardier by the Government of Canada. The Panel rejected Brazil's argument, finding instead that "[w]e 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." We note that this finding was appealed by either Brazil or Canada. Even if we were to assume that the "matching" provisions of the apply in this case (an argument Brazil did not make), those provisions clearly do not allow a comparison to be made between the net interest rates applied as a consequence of subsidies granted by a particular Member and the total amount of subsidies provided by another Member. We also note that under PROEX, the interest rate equalisation subsidies for regional aircraft are provided at an "across-the-board" rate of 3.8 per cent for export sales transactions.[footnote omitted] That rate is fixed, and does not vary depending on the total amount of subsidies provided by another Member to its regional aircraft manufacturers. Thus, we cannot accept Brazil's argument that the export subsidies for regional aircraft under PROEX should be "permitted" because they "match" the total subsidies provided to Bombardier by the Government of Canada.

6.83 The text of the Appellate Body decision reveals elements that support the view of Canada in respect of the role of the CIRR. The language used by the Appellate Body in several places suggests that the CIRR is the sole and immutable benchmark against which material advantage is to be assessed. In particular, the Appellate Body's statement, in paragraph 182 of its Report, that "the appropriate comparison to be made in determining whether a payment is "used to secure a material advantage", within the meaning of item (k), is between the actual interest rate applicable in a particular export sales transaction after deduction of the government payment (the " interest rate") and the relevant CIRR", is on its face absolute and would not allow of another benchmark. Similarly, in paragraph 183 the Appellate Body Report states, somewhat categorically, that, "[i]n light of our analysis, it was for Brazil to establish a

recipient.[82] Rather, the Appellate Body merely found that such an advantage had to be "material" and, if the net interest rate was below CIRR, this was irrebutable evidence that the advantage was in fact "material".[83] Under this reading of the Appellate Body Report, if we understand it correctly, a PROEX payment resulting in an export credit at an interest rate above CIRR would still be used to secure a "material" advantage if it resulted in an export credit on "materially" better terms than the terms that would otherwise have been available in the marketplace .[84] Given Canada's references in this context to purely commercial transactions – , transactions not benefiting from official support – we assume that Canada defines the "marketplace" to mean the purely commercial marketplace. Consistent with this interpretation, and in support of its position that the advantage conferred by PROEX payments is "material", Canada submitted affidavits from airlines indicating that a reduction in interest rates of as little as 25 basis points could have a material impact on their choice of aircraft.

6.89 We cannot however interpret the Appellate Body Report in this manner. If the Appellate Body meant what Canada now suggests it meant, there would have been no need for it to have referred to the CIRR in order to establish that the advantage in question was "material". In this respect, we recall that, under PROEX, a borrower negotiates the best interest rate it can obtain in international financial markets, and then benefits from a buy-down of that interest rate of 2.5 percentage points (3.8 percentage points under PROEX as it existed at the time of the original Panel Report). There was information in the record indicating that this interest rate buy-down reduced the total cost of an aircraft to a borrower by several million dollars[85], and in any event there could be little doubt that a 3.8 percentage point reduction in the interest rate on a long-term export credit would secure a "material" advantage in the field of export credit terms, the point of comparison were in fact the terms otherwise available to that borrower in the commercial marketplace. Thus, the Appellate Body could have noted the failure of the Panel to consistently state than an advantage had to be "material", but concluded on the basis of the record that the amount of the PROEX payments could not but be used to secure a material advantage. The fact that the Appellate Body did not indicates to us that they considered the Panel's basic approach to be incorrect.

6.90 Brazil, by contrast, argues that "the appropriate reference for determining whether a material advantage is secured is the 'marketplace' and not a specific transaction".[86] In referring to the "marketplace", Brazil apparently means that a payment does not secure a material advantage if the net interest rate on the export credits is no lower than that which is available to purchasers of competing regional aircraft. In light of the "evidence" cited by Brazil (paras. 6.94 and 6.97,) regarding interest rates in respect of regional aircraft, we conclude that Brazil would not distinguish between commercial and non-commercial benchmarks in determining what interest rates prevailed in the "marketplace". Put simply, Brazil's position seems to be that its payments do not secure a material

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[82] , a payment is used to secure a material advantage where the payment has resulted in the availability of an export credit on terms that are materially more favourable than the terms that would otherwise have been available in the marketplace .

[83] Thus, Canada asserts that, "in the unlikely event that PROEX results in a net interest rate that is above CIRR, such a rate still secures a 'material advantage' . . . . By its design, PROEX secures a material advantage". Response of Canada to Question 7 of the Panel.

[84] Oral Statement of Canada at the Meeting of the Panel, paras. 97-98 ("[I]f a net interest rate is below the relevant CIRR, the 'payment' in question must be considered to have secured a material advantage. If, however, a net interest rate is above the CIRR, a party that claims the benefit of an exception, if such an exception existed, would have the burden of establishing that it does not secure a material advantage as compared to the prevailing market rate . . . This is because an interest rate buy-down of 2.5 percentage points may well not bring the net interest rate in a transaction below the relevant CIRR in cases . But, it would be untenable to argue that such a massive subsidisation would not, at the same time, secure a material advantage."(emphasis added).

[85] A report by Ernst and Young estimated that the net present value of the equalisation payments would total $2,454,162 per aircraft (Exhibit 23 to First Submission of Canada in the original dispute).

[86] First Submission of Brazil, para. 4.

advantage provided that the resulting net interest rate is no lower than the interest rates available in respect of export credits for competing regional aircraft, irrespective of whether those interest rates are the result of market forces or government intervention.

6.91 In our view, however, Brazil's approach is also inconsistent with the choice of CIRR as benchmark by the Appellate Body. The Appellate Body seems to have identified the CIRR as a relevant benchmark under the material advantage clause because it represents the " commercial interest rate" faced by a potential borrower in respect of a particular currency. In this respect, we note that, under the , the CIRR is established according to a number of principles, including that the CIRR should represent final commercial lending interest rates in the domestic market of the currency concerned, that it should closely correspond to the rate for first-class domestic borrowers and to a rate available to first-class foreign borrowers and that it should not distort domestic competitive conditions.[87] In other words, the CIRR is intended in principle to approximate the interest rate that first-class borrowers would pay "commercially", , in private transactions not benefiting from official support. The reasoning of the Appellate Body in choosing the CIRR seems to have been that a payment would be used to secure a advantage, as opposed to an advantage that was not material, if it resulted in an interest rate that was below the lowest interest rates available to the best borrowers in respect of a particular currency, irrespective of whether that rate would have been available to the borrower in question.

6.92 For the foregoing reasons, we consider that a Member may under the first paragraph of item (k) as interpreted by the Appellate Body establish that a payment was not used to secure a material advantage in the field of export credit terms, even if it resulted in a below-CIRR interest rate, if it could establish that the net interest rate resulting from the payment was not lower than the minimum interest rate in respect of that currency.[88]

6.93 That being the case, the next question we must address is whether Brazil has demonstrated that the benchmark it has chosen as the floor net interest rate for export credits supported by PROEX payments is in fact equal to or higher than the "minimum commercial interest rate" available in the marketplace. In considering this question, we recall that Brazil is seeking to use the first paragraph of item (k) as an affirmative defence and that it therefore bears the burden of establishing entitlement to it.[89] At the same time, and conscious that Canada might have access to relevant information not in the possession of Brazil, we have exercised our authority to seek certain information from Canada,[90] and we have taken the responses of Canada into account when examining this issue.

6.94 The first piece of evidence relied on by Brazil in support of the view that there are commercial interest rates below CIRR is documentation relating to the terms of an export financing transaction at a floating interest rate for large civil aircraft supported by export credit guarantees from the United States Export-Import Bank. Brazil compared the interest rate on this transaction (LIBOR plus 3 basis points) plus an amount to reflect a one-time guarantee fee it estimated to have been charged by the Export-Import Bank, to the "minimum" net interest rate for export credits benefiting

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[87] , Article 15.

[88] We note that it would make little sense to compare the interest rate on a floating rate loan with the CIRR when determining whether an export credit or payment was "used to secure a material advantage in the field of export credit terms". We assume that in such circumstances the issue of material advantage would be assessed on the basis of the minimum commercial interest rate for comparable floating-interest rate export credits.

[89] Original Panel Report, para. 7.17. Of course, we have determined that the first paragraph of item (k) cannot be used to establish that a measure is "permitted" (para. 6.67,). If a complainant sought to use the first paragraph of item (k) to establish that a measure was , the complainant would, as in all cases, bear the initial burden of presenting evidence and argument sufficient to establish a case of violation. , Report of the Appellate Body adopted on 13 December 1998, WT/DS26/AB/R, WT/DS48/AB/R, para. 98.

[90] Responses of Canada to Questions 4 and 5 of the Panel.

from PROEX payments (10-year US Treasury Bonds plus 20 basis points) and concluded that the "minimum" net interest rate for PROEX-supported export credits was higher than that of the Export-Import Bank-supported transaction. Brazil further argued that this transaction appeared to involve a Chinese purchaser, and that the guarantee fee in respect of airline borrowers from developed countries such as Switzerland would be lower. In Brazil's view, this example demonstrates that the marketplace supports interest rates below the "minimum" net interest rate for export credits supported by PROEX payments, and that PROEX payments therefore are not used to secure a material advantage in the field of export credit terms.

6.95 Canada challenges the relevance and comparability of the transaction referred to by Brazil. First, it argues that this transaction involves a loan guarantee, rather than direct financing. It considers that , because the first phrase of the first paragraph of item (k) refers to direct export credit financing, it would be incongruous if "the field of export credit terms" in the second clause of that paragraph included loan guarantees. In other words, Canada seems to be arguing that, in determining whether a payment is used to secure a material advantage in the field of export credit terms, export credits supported by government guarantees cannot be taken into account. We agree with Canada, but not for the reasons it has expressed in this dispute. It seems clear to us that the fact the export credit terms in question here are the result of a guarantee is of little relevance.[91] On the other hand, the fact that these terms are the result of a guarantee is highly relevant, if we are correct that, in order to justify a benchmark below CIRR, Brazil must demonstrate that the marketplace supports interest rates as low as the rate for 10-year US Treasury Bonds plus 20 basis points. Clearly, Brazil has not demonstrated that the interest rate on this financing transaction, which is the direct result of a government guarantee, is a commercial or market rate of interest.

6.96 In any event, the financing transaction relied upon by Brazil is a floating-rate transaction, while the "minimum" net interest rate set by Brazil in respect of export credits supported by PROEX payments relates to transactions at fixed interest rates.[92] In response to a question from the Panel as to how Brazil's benchmark rate would be applied in the case of floating interest rate transactions, Brazil explained that there are no records that PROEX transactions for aircraft have involved floating interest rates, nor are such transactions anticipated. Brazil further stated that it has not determined what "floor" rate it would apply if it provided PROEX payments in support of floating interest rate transactions, although it would have to be compatible with market rates.[93] Under these circumstances, it is hard to understand what relevance the terms of a floating interest rate transaction might have for the case at hand.

6.97 The second piece of "evidence" cited by Brazil involves a legal issue related to the application of the known as "market windows". As noted earlier in this Report, the gist of the market windows argument is the view of Canada that an export credit agency, such as the Export Development Corporation, under certain circumstances is not providing "official support", and is therefore not subject to the . It may therefore under certain circumstances provide export credits on terms more favourable than those envisioned by the (e.g., at an interest rate below CIRR). Brazil relies on this fact as evidence that Canada may provide export credits for regional aircraft at rates which are below the CIRR, and argues that under these circumstances Brazil as well should be entitled to support through PROEX payments export credits at a net interest rate below CIRR.

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[91] For example, a parent company might guarantee an export credit of a subsidiary, thereby allowing the subsidiary to borrow at a lower interest rate.

[92] Because a fixed interest rate locks in the lender for the duration of the export credit, lenders typically charge higher interest on a fixed interest rate loan than on a floating interest rate loan. Thus, it makes little sense to compare fixed interest rates to floating interest rates.

[93] Response of Brazil to question 8 of the Panel.

6.98 Based on our understanding of the Appellate Body's Report, the fact that Canada considers itself entitled to provide through its Export Development Corporation export credits on terms that are more favourable than those allowed by the is not in itself a reason to conclude that Brazilian payments resulting in net interest rates comparable to those offered by Canada were not used to secure a material advantage in the field of export credit terms. After all, and for the reasons set forth in para. 6.65 of this Report, any export credits provided by the EDC in respect of regional aircraft at an interest rate below CIRR are not protected by the safe harbour of the second paragraph of item (k). Accordingly – and in light of our view that Members cannot use the first paragraph of item (k) to establish that a subsidy is "permitted" – Brazil would be free to challenge any such export credits to the extent that they were subsidies within the meaning of Article 1 that are contingent upon export performance within the meaning of Article 3.1(a), just as Canada could challenge any export credits on the same basis.

6.99 We were, however, struck by Canada's assertion that export credits provided by EDC through the "market window", even at interest rates below CIRR, were nevertheless "commercial" export credits that did not confer a benefit within the meaning of Article 1. Assuming this were the case, then, applying the Appellate Body's reasoning as we understand it, the existence of these "commercial" interest rates at below CIRR would mean that Brazil could itself provide PROEX payments resulting in below-CIRR net interest rates without securing a material advantage and therefore not fall within the scope of the prohibition.[94] Accordingly, and in light of the fact that information regarding the terms of EDC export credits was in the sole control of Canada, the Panel asked Canada to indicate whether any Canadian government agency, including EDC, had provided export credits in respect of regional aircraft at an interest rate below CIRR since 1 January 1998 and, if so, to indicate the interest rates at which such export credits were provided.

6.100 Canada responded that it has since 1 January 1998 provided export credits in respect of regional aircraft at interest rates below CIRR.[95] Although it does not identify the aircraft financed, the borrowers or the precise terms and conditions of these transactions, it does provide certain information in respect of them. In particular, we know that these transactions involved direct financing (as opposed to guarantees) and that they involved fixed interest rates.

6.101 Canada informs us that one of these transactions was a Canada Account transaction which involved "matching". Although Canada asserts that this transaction "was implemented in full compliance with the ", it does assert that this transaction was in any sense a market-based transaction.

6.102 Canada further confirms that "there were instances where certain of EDC's financing transactions were at a rate less than the CIRR applicable on the date the transaction closed." Canada does not specify the number of such below-CIRR transactions, nor the share of EDC's regional aircraft transactions made at below-CIRR interest rates. It does however insist that these transactions were "market-based and commensurate with the risk associated with the particular borrower, and said transactions included customary collateral security protection". Canada explains in some detail that the situation of below-CIRR market rates can arise because the CIRR lags behind the market. Thus, in cases where interest rates are falling, the market rate at the time a transaction is closed can be lower than the CIRR, which is constructed on the basis of bond rates in an earlier period. For example, the

[94] Canada asserts that in

CIRR applicable to transactions closing during the period 15 September – 15 October would be constructed using the average of the 7-year Treasury for the month of August, plus 100 basis points. Accordingly, Canada concludes, "[t]o an entity that operates on the basis of market principles, the calculation of the CIRR is such that it would not be considered a reliable reflection of current market conditions." Finally, Canada categorically asserts that, with the exception of the Canada Account transaction, the interest rate "in every case has been well above Brazil's preferred PROEX rate of 10-year Treasury plus 20 basis points."

6.103 We are not in a position to perform an independent assessment as to whether the below-CIRR export credits provided by Canada in respect of regional aircraft were or were not at commercial rates, as Canada has not provided us with any details concerning the specific terms and conditions of the transactions in question. Nevertheless, in light of Canada's clear admission not only that there can be commercial interest rates below CIRR but also that Canada itself has provided export credits in respect of regional aircraft at such below-CIRR "commercial" interest rates, we conclude that payments in respect of export credit financing for regional aircraft at below-CIRR interest rates are not necessarily used to secure a material advantage in the field of export credit terms as that term has been interpreted by the Appellate Body.

6.104 That said, the ultimate question in this dispute is not whether below-CIRR commercial interest rates in respect of regional aircraft financing may be said to involve a material advantage, but whether Brazil has demonstrated that PROEX payments aimed at achieving the benchmark rate set by Brazil – a net interest rate on fixed interest rate export credits based on the 10-year US Treasury Bond plus 20 basis points – are not used to secure a material advantage in the field of export credit terms. We recall that the benchmark established by Brazil in respect of export credits supported by PROEX payments is below the relevant CIRR, and we note in addition that Brazil has presented evidence that export credits at fixed interest rates in respect of regional aircraft[96] are being provided in the market to any borrower at the benchmark rate of 10 year US Treasury bonds plus 20 basis points established by Brazil. We recall that, because Brazil is seeking to assert an "affirmative" defence, and that it bears the burden of demonstrating entitlement to that defence. We further note that, in respect of access to information regarding commercial interest rates – and with the exception of information regarding export credits provided by EDC at rates alleged by Canada to be "commercial" – such information is equally accessible to Brazil and Canada.

6.105 In respect of that information which is in the exclusive possession of Canada, Canada has categorically stated that, with the exception of one Canada Account transaction which clearly is commercial, all fixed interest rate export credit financing provided by Canadian government agencies, including EDC export credits at rates below CIRR, has been at rates "well above" the Brazilian benchmark. We cannot assume bad faith on the part of Canada and therefore must accept the veracity of these statements.[97]

6.106 For the foregoing reasons, we find that Brazil has failed to demonstrate that PROEX payments are not "used to secure a material advantage in the field of export credit terms" within the meaning of the first paragraph of item (k).

(c) Conclusions and closing remarks

In this section of our Panel Report, we have found that:

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[96] Or, for that matter, any aircraft. As noted in paras. 6.92 – 6.95 of this Report, the only evidence presented by Brazil relevant to the interest rates in respect of export credits for aircraft involved non-commercial, floating interest rates.

[97] , Report of the Appellate Body adopted on 12 January 2000, WT/DS87/AB/R-WT/DS/110/AB/R, para. 74.

(i) PROEX payments in respect of regional aircraft pursuant to the PROEX scheme as modified are subsidies contingent upon export performance within the meaning of Article 3.1(a) of the ;

(ii) Brazil has failed to demonstrate, both as a matter of law and as a matter of fact, that PROEX subsidies are "permitted" by the first paragraph of item (k). In this respect, we recall our finding that the first paragraph of item (k) cannot be used to demonstrate that a subsidy contingent upon export performance within the meaning of Article 3.1(a) is "permitted". We further recall our findings that Brazil has failed to establish (a) that PROEX payments are "payments" within the meaning of the first paragraph of item (k); and (b) that PROEX payments are not "used to secure a material advantage in the field of export credit terms".

Therefore, we conclude that PROEX payments in respect of regional aircraft under the PROEX scheme as modified by Brazil are export subsidies prohibited by Article 3 of the . Accordingly, we conclude that in this respect Brazil has failed to implement the recommendation of the DSB that it withdraw the export subsidies for regional aircraft under PROEX within 90 days.

6.107 We note that Brazil's effort to defend PROEX payments as "permitted" under the first paragraph of item (k) of the Illustrative List centred on the notion that a developing country Member had to be "permitted" by that paragraph to provide otherwise prohibited export subsidies in order to meet WTO-consistent competition from developed country Members in the field of export credit terms. In our view, however, the as properly interpreted establishes a level playing field for all Members in respect of export credit practices (except, of course, to the extent that a Member is exempted from the export subsidy prohibition by reason of special and differential treatment). Under these circumstances, if a developing country Member (or indeed any Member) encounters an export credit that has been provided on terms that it cannot meet consistent with the , the proper response is to challenge that export credit in WTO dispute settlement.[98]

7.1 For the reasons set forth in this Report, we conclude that Brazil's measures to comply with the Panel's recommendation either do not exist or are not consistent with the . Accordingly, we conclude that Brazil has failed to implement the DSB's 20 August 1999 recommendation that it withdraw the export subsidies for regional aircraft under PROEX within 90 days.

7.2 Canada requests that we suggest, pursuant to Article 19.1 of the that the parties develop mechanisms that would allow Canada to verify compliance with the original recommendation of the DSB. Canada notes that Brazil has a reciprocal interest in verifying Canada's compliance in a parallel dispute, .[99] Canada emphasises that it is seeking a continuing role for the Panel in proposing such verification procedures, nor is it requesting that we impose such procedures. Brazil responds that, although it does not in principle oppose an agreement with Canada on reciprocal transparency, it does not consider that it is an appropriate matter for a suggestion under Article 19.1 of the , but is better left to be agreed by the parties. Brazil notes that any such agreement would have to involve balanced and truly reciprocal offers of transparency.

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[98] In this regard, we recall the statement of the Appellate Body in that: "we do not intend to suggest that Brazil is precluded from pursuing another dispute settlement complaint against Canada, under the provisions of the and the concerning the consistency of certain of the EDC's financing measures with the provisions of the ."

[99] First Submission of Canada, para. 45.

7.3 We note that Article 19.1 provides that "the panel . . . may suggest ways in which the Member concerned could implement the recommendation". In our view, Article 19.1 appears to envision suggestions regarding what could be done to a measure to bring it into conformity or, in case of a recommendation under Article 4.7 of the