ANNEX B

SUBMISSIONS OF BRAZIL

Oral statement of Brazil

I. INTRODUCTION

1. On 4 August 2000, the Dispute Settlement Body ("DSB") adopted the report of the Appellate Body in the previous Article 21.5 proceedings in this matter.[1] In its report, the Appellate Body found that Brazil had failed to establish that the steps it had taken to amend the measure at issue in this case, the *Programa de Financiamento às Exportações* (PROEX), brought that measure into conformity with the previous rulings and recommendations of the DSB. Accordingly, on 12 December 2000, Brazil advised the DSB of additional amendments to PROEX that it had taken to bring the measure fully into conformity with Brazil's obligations under the *Agreement on Subsidies and Countervailing Measures* (the "SCM Agreement" or "Agreement").

2. On 19 January 2001, Canada notified the DSB of its intention once again to seek recourse to Article 21.5 of the *Understanding on Rules and Procedures Governing the Settlement of Disputes* ("DSU") in these proceedings. Canada's decision not to seek consultations concerning the steps Brazil had taken to amend PROEX has meant that Brazil has not had an opportunity to explain the measure to Canada. At its meeting on 16 February 2001, the DSB referred the matter to the original Panel.

3. In this submission, Brazil will demonstrate first, that PROEX interest rate support payments for aircraft no longer constitute a subsidy within the meaning of Article 1 of the SCM Agreement. Assuming *arguendo*, however, that PROEX interest rate support payments are a subsidy within the

Letter No. 002881 sets the maximum allowable interest equalization payment at 2.5 percent.[9] This maximum amount is subject to the stipulation of Article 1, paragraph 1 of Resolution 00279 that

"in connexion with the conclusion of the treaty." It can hardly be disputed that all WTO agreements – including the Marrakesh Agreement itself, and the DSU – provide the context for the proper interpretation of the SCM Agreement.

26. The process of amendment is extremely important in the WTO Agreement, as it is in any treaty. The terms of a treaty are carefully negotiated, and are not changed lightly or casually. Article X of the Marrakesh Agreement reflects the importance of amendments to the WTO by providing a detailed and precise system for their adoption, a system designed to protect the interests of all Members.

27. Article X:1 of the Marrakesh Agreement specifies that a decision even to submit a proposed amendment to the Members shall itself be taken by consensus of the entire WTO membership. If consensus is not reached within a specified period, the decision whether to submit a proposed amendment shall be taken by a two-thirds majority of the Members. If the two-thirds majority decides to submit the amendment to the Members, paragraph 3 provides that, in most circumstances, if two-thirds accept, the amendment shall take effect only as to those that have accepted it.

28. Article X:3 of the Marrakesh Agreement further requires that any amendments to an Agreement in Annex IA (which includes the SCM Agreement) "that would alter the rights and obligations of the Members" take effect only "for the Members that have accepted them." The only

second paragraph is an interpretation that leads, in the words of Article 32(b) of the Vienna Convention, "to a result which is manifestly absurd and unreasonable."

40. Accordingly, for all these reasons, Brazil submits that the Panel must examine the issue of whether PROEX III is in conformity with the interest rate provisions of an international undertaking on official export credits by reference to the text of the 1992 version of the *OECD Arrangement*, not any later version.

B. PROEX III IS IN FULL CONFORMITY WITH THE RELEVANT INTEREST RATE PROVISIONS OF THE 1992 *OECD ARRANGEMENT*

41. The second paragraph of item (k) makes reference only to the "interest rates provisions" of the *Arrangement*, not to the provisions governing the terms and conditions of export credits, which are broader. The interest rates provisions of the 1992 *Arrangement* are those set out in Article 5 of the main text and Article 21 of Annex IV: Sectoral Understanding on Export Credits for Civil Aircraft.[22] PROEX III conforms with these provisions of the *Arrangement.* Brazil does not agree with the approach of the Panel in *Canada – Aircraft*, which used a broad approach to identify what it believed were the interest rates provisions of the 1998 *OECD Arrangement.*[23] However, even if the same broad approach is applied to the 1992 *OECD Arrangement*, Brazil conforms with the corresponding interest rates provisions: Articles 3 through 7 of the main text, and Articles 17 through 22 and Articles 24 and 25 of Annex IV. Brazil, under PROEX III, applies in practice those provisions of the 1992 *OECD Arrangement* as required by the second paragraph of item (k).

42. PROEX III conforms with the 1992 *OECD Arrangement* because all PROEX III supported transactions in the regional aircraft sector take the form of official financing support with a repayment term of two years or more, as required by Article 1 of the *Arrangement.*

43. PROEX III complies with Article 3 of the *Arrangement*, which requires that purchasers make cash payments equal to a minimum of 15 percent of the export contract value; the maximum percentage allowed under PROEX III for the purpose of interest rate equalization is 85 percent of the export value of the sale.[24]

44. Article 4 of the *Arrangement* relates to the terms of repayment. However, pursuant to Articles 1(b) and 9(d) of the *Arrangement*, these provisions are superseded by Article 21 of Annex IV dealing specifically with the aircraft manufactured by Embraer. PROEX III is in conformity with the provisions of that Article, as discussed below.

45. Article 5(a) of the *Arrangement* fixes the minimum interest rate at the relevant CIRR. The official financing support to the regional aircraft industry under PROEX III is at fixed interest rates only.[25] The net interest rates of all transactions in the regional aircraft sector under PROEX III are at or above the relevant CIRR.[26]

46. Articles 6 (Local Costs) and 7 (Maximum Period of Validity of Commitments, Prior Commitments and Certain Aid Commitments) are not relevant to PROEX III because no aircraft credits are granted, financed, refinanced, guaranteed or insured under PROEX III. Article 1 of Resolution 002799 explicitly states that PROEX III provides only interest rate support "enough to render financing costs compatible with those practiced in the international market" and that the financing to the regional aircraft industry is in the form of interest rate support in compliance with the

[22] The text of the 1992 *OECD Arrangement* is attached as Exhibit Bra-7.
[23] *Canada -- Aircraft* 21.5 Report, para. 5.147(d).
[24] Article 5 of Directive No. 374.
[25] Article 1, para. 2 of Resolution No. 002799.
[26] Article 1, para. 1 of Resolution No. 002799. As will be discussed below, the SDR-based rates referred to in Article 5(b) of the *Arrangement* are no longer relevant.

CIRR.[27] Moreover, Article 5 of Directive 374 explicitly limits the interest rate support to 85 percent of the export value of the contracted sale, thus clearly excluding additional local costs.

47.

PROEX III conforms to all of these provisions, including both the minimum interest rates and "all other applicable" provisions of the 1998 *OECD Arrangement* that "operate to support or reinforce the minimum interest rate"[32] with one arguable exception.

55. PROEX III transactions are official financing support with a repayment term of two years or more, as required by Article 2 of the 1998 *Arrangement*

61. First, Brazil disagrees with the *Canada – Aircraft* Panel and believes that Article 29 is not an interest rate provision. The interest rates provisions of the 1998 *Arrangement* are Articles 15 through 19 of the main text and Article 22 of the Annex. PROEX III fully conforms with those provisions. While Article 6 of Directive 374 gives the Committee the discretion to finance up to 20% of the spare parts included in a transaction, the Committee is not required to do so and will not do so with respect to regional aircraft because of the insignificant percentage of the value of the spare parts included in regional aircraft export sales.[36] This is a discretionary, not a mandatory, provision. Brazil, therefore, in practice applies the interest rates provisions of the 1998 *Arrangement.*

62. For all these reasons PROEX III conforms with all the provisions of the 1998 *Arrangement* and its relevant Sector Understanding that the *Canada –Aircraft* Panel described as reinforcing the minimum interest rate for Brazil's regional jet transactions and hence as the "interest rate provisions" of that *Arrangement.* The Panel should therefore find that PROEX III qualifies for the "safe haven" of the second paragraph of item (k).

VI. PROEX III IS NOT USED TO CONFER A MATERIAL ADVANTAGE WITHIN THE MEANING OF ITEM (K) FIRST PARAGRAPH

63. Brazil has demonstrated that PROEX does not confer a benefit within the meaning of Article 1 of the SCM Agreement, and therefore is not a subsidy. Brazil also has demonstrated that, assuming *arguendo* that PROEX is a subsidy – it [illegible] Wafe [illegible] 0 -12.75 TD [illegible] 0 it

B. AN *A CONTRARIO* INTERPRETATION OF ITEM (K) FIRST PARAGRAPH IS REQUIRED

66. Brazil submits that the material advantage clause should be interpreted *a contrario* such that a payment that is *not* used to secure a material advantage within the meaning of the first paragraph is *not prohibited*, and is therefore *permitted*, under the SCM Agreement. The failure to permit an *a contrario* interpretation effectively would render the material advantage clause inutile, contrary to the customary rules of interpretation of public international law.

67. In reviewing this issue in the original Article 21.5 proceedings, the Appellate Body began its analysis by considering whether PROEX II in fact conferred a material advantage.[38] As noted above, the Appellate Body concluded that Brazil had not discharged its burden of showing that PROEX III did not confer a material advantage. Regarding Brazil's *a contrario* argument, however, the Appellate Body went on to say that if Brazil had discharged this burden, the Appellate Body *"would have been prepared to find"* that an *a contrario* interpretation of the material advantage clause could be used to justify PROEX payments.[39] Thus, as a legal matter, the Appellate Body appears to take the view that assuming the other legal conditions are met, the first paragraph of item (k) should be read *a contrario* to permit a subsidy that does not confer a material advantage. This Panel should reach the same conclusion.

C. PROEX IS A "PAYMENT" WITHIN THE MEANING OF ITEM (K) FIRST PARAGRAPH

68. PROEX III interest rate support is a "payment by [Brazil] of all or part of the costs incurred by exporters or financial institutions in obtaining credits" within the meaning of item (k) first paragraph.

69. Neither exporters nor financial institutions wish to obtain credits in order to hoard them; they wish to "obtain" credits only to "provide" them. Before credits can be provided, they must be obtained – obtained at a cost, and, in the case of a developing country like Brazil, a considerable cost.

70. When the lending institution is outside of the country, Embraer, the Brazilian exporter, faces costs in obtaining for its customer a financial package that is competitive in the market, including a market in which "market window" operators, such as Canada, are offering rates below the CIRR. If Embraer could not obtain a competitive financial package for its customer, it would be forced to take other costly action, such as paying for a commercially-available loan guarantee at a high premium. When the lender is inside the country, however, it is the lender itself – the bank in Brazil – that must obtain dollars in the market in order to provide dollar credits. This analysis was effectively confirmed by the original Article 21.5 Panel, which observed that "developing countries' costs of borrowing are almost inevitably higher than those of developed counties."[40]

71. PROEX interest rate support payments are payments designed to offset, at least partially, the added costs faced by Brazilian institutions in obtaining the credits they provide.

72. If PROEX payments do not fit the definition of "payments" contemplated by item (k), it is impossible to contemplate exactly what kind of payments in the export credit field the drafters of this provision had in mind. The original Article 21.5 Panel stated that "a payment by Brazil that allowed a Brazilian financial institution to provide export credits" could be permitted under the first paragraph of item (k).[41] This Panel should follow the logic of that statement and find that PROEX III payments are "payments" within the meaning of the first paragraph of item (k).

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[38] *Id*., para. 58.
[39] *Id*., para. 80.
[40] Original 21.5 Report, para. 6.73.
[41] Original 21.5 Report, para. 6.44.

VII. CONCLUSION

73. Brazil does not understand Canada's purpose in again seeking recourse to Article 21.5, especially without first seeking consultations with Brazil on its concerns regarding PROEX III. As noted above, Canada has previously described its purpose in these proceedings as seeking to ensure that Brazil would provide PROEX support only at or above the CIRR. As the Panel is aware, Brazil is of the view that – as, indeed, Canada has admitted – transactions in the regional jet market occur below the CIRR, and that Brazil should therefore not have to comply with standards that are honoured more in breach than in observance by the group of developed country Members who themselves developed those standards. Nevertheless, in response to the rulings and recommendations of the DSB, Brazil has complied with Canada's stated wishes and conformed PROEX to the interest rate provisions of the *Arrangement*, as required by the second paragraph of item (k) of the SCM Agreement. The sole issue before this Panel is whether the regulations governing PROEX conform to the relevant provisions of the *Arrangement.* The Panel should answer this question in the affirmative and not yield to Canada's efforts once more to move the goalposts for Brazil.

74. Accordingly, Brazil requests that the Panel find and determine that Canada has not established that PROEX III confers a benefit within the meaning of Article 1 of the SCM Agreement and, accordingly, that Canada has not sustained its burden of proving that PROEX III is a subsidy.

75. However, even if the Panel should find that PROEX is a subsidy within the meaning of Article 1, contingent upon export within the meaning of Article 3, PROEX is nevertheless not prohibited because:

(a) Brazil in practice applies the interest rates provisions of the relevant undertaking – the 1992 version of the *Arrangement on Guidelines for Officially Supported Export Credits* of the OECD;

(b) Brazil in practice applies the interest rates provisions of the 1998 version of the *Arrangement on Guidelines for Officially Supported Export Credits* of the OECD;

(c) PROEX interest rate support is not used to provide a material advantage in the field of export credit terms.

LIST OF EXHIBITS

BRA-1. Resolution No. 002799 of the Central Bank of Brazil, 6 December 2000 (Portuguese and English versions)

BRA-2. Circular letter No. 002881 of the Central Bank of Brazil, 19 November 1999 (Portuguese and English versions)

BRA-3. Directive No. 374 of the Ministry of Development, Industry and Foreign Trade, 21 December 1999, and selected pages of the Annex thereto (Portuguese and English versions)

BRA-4. Printout of http://222.eksportfinans.no/eprise/main/EF/content/english/Inngangs

BRA-5. David Stafford, *Wallen, Helsinki, Schaerer et al.: Some Major Achievements, Some Challenges to Meet*, in THE EXPORT CREDIT ARRANGEMENT, ACHIEVEMENTS AND CHALLENGES 1978-1998 (OECD, 1998)

BRA-6. Presentation by Mr. Fumio Hoshi, Director-General, International Finance Policy Department, Japan Bank for International Cooperation, at the EXIMBANK 65th Anniversary Conference, May 2000

BRA-7. 1992 *OECD Arrangement* on Guidelines for Officially Supported Export Credits

BRA-8. Summary of The Schaerer Package, in THE EXPORT CREDIT ARRANGEMENT, ACHIEVEMENTS AND C,

ANNEX B-2

SECOND SUBMISSION OF BRAZIL

(23 March 2001)

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II. QUESTION PRESENTED

6. The question presented to this Panel is "whether the measures taken by Brazil to comply with the rulings and recommendations of the DSB bring Brazil into conformity with the provisions of the SCM Agreement and result in the withdrawal of the export subsidies to regional aircraft under PROEX."[6]

7. During the Article 22.6 Arbitration proceedings,[7] Canada was authorized to suspend concessions to Brazil in the amount of C$344.2 million per year as appropriate countermeasures within the meaning of Article 4.10 of the SCM Agreement. This authorization was based on a calculation of the amount of subsidies under PROEX I and II deemed to be prohibited in the previous Panel proceedings. Accordingly, Brazil distinguishes between the so-called "undelivered aircraft" – aircraft subject to the calculation of the level of authorized countermeasures in the Article 22.6 proceedings – and any new PROEX III commitments. Brazil has stated repeatedly that it is unable to default on commitments it made to private parties who have relied, in good faith, on Brazil's commitments for the undelivered aircraft. The sole issue before this Panel, therefore, is whether PROEX III now complies with the requirements of the SCM Agreement for new orders.

III. BURDEN OF PROOF

8. In its submission, Canada asserts that it has presented evidence that satisfies its burden of proving that payments under PROEX III "continue to be prohibited export subsidies."[8] Canada has done nothing of the kind.

9. Under the standard articulated by the Appellate Body in *Chile – Alcoholic Beverages*, PROEX III enjoys a presumption of compliance:

IV. LEGAL ARGUMENT

A. CANADA HAS NOT ESTABLISHED THAT PROEX III INTEREST EQUALIZATION PAYMENTS FOR AIRCRAFT CONSTITUTE A SUBSIDY

11. Canada claims that "Brazil continues to acknowledge that PROEX [III] subsidies are prohibited export subsidies."[12] This statement is incorrect. Brazil acknowledges no such thing. Canada's added claim, in footnote 22 to its First Submission, that Brazil has acknowledged that PROEX payments were "prohibited export subsidies" also is incorrect. Brazil has acknowledged nothing of the sort. What Brazil has argued in the past is that PROEX interest equalization payments, as they were constituted in the prior proceedings, were subsidies contingent upon export, but that they

reasons explained in its First Submission, submits that PROEX III conforms with the relevant interest rate provisions of the *Arrangement* and therefore qualifies for the safe haven of the second paragraph of item (k). Brazil also believes, however, that PROEX III is not used to secure a material advantage within the meaning of item (k) first paragraph. Brazil explains why this is so in this section of its submission.

16. Brazil agrees with Canada that in order to prevail under item (k) first paragraph, Brazil must establish three elements.[18] First, Brazil must show that item (k) first paragraph may be interpreted *a contrario* such that a payment that is *not* used to secure a material advantage within the meaning of the first paragraph is *not prohibited*, and therefore is *permitted*, under the SCM Agreement. Second, Brazil must show that PROEX III payments fall within the definition of "payment by [a government] of all or part of the costs incurred by exporters or financial institutions in obtaining credits," within the meaning of the first paragraph of item (k). Third, Brazil must show that PROEX payments are not used to "secure a material advantage in the field of export credit terms." Canada's arguments on each of these three points are unavailing, and the Panel should find that PROEX III payments are not prohibited export subsidies.

2. The First Paragraph of Item (k) Must Be Given an *A Contrario* Interpretation

17. Item (k) of Annex I to the *SCM Agreement* provides, in relevant part, that certain governmental payments are prohibited export subsidies "in so far as they are used to secure a material advantage in the field of export credit terms." The addition of this "material advantage" clause where the paragraph would otherwise conclude necessarily affects the meaning of the paragraph. For the following reasons, the Panel should interpret this clause to mean that payments *not* used to secure a material advantage are *not* prohibited.

(b) Standard Principles of Treaty Interpretation Favor Brazil's Interpretation

18. The first paragraph of item (k) should be interpreted in accordance with the provisions of Article 31 of the *Vienna Convention on the Law of Treaties* (the "Vienna Convention"), which provides that a treaty shall be interpreted in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in light of its object and purpose. Moreover, this Panel "must give meaning and effect to all the terms of the treaty."[19] While these principles appear straightforward, there nevertheless remains considerable dispute as to the "ordinary meaning" of the material advantage clause.

19. In Brazil's view, the issue is quite simple. The Panel must give meaning and effect to the material advantage clause. The minimum meaning and effect that can reasonably be given is that the clause qualifies the preceding language of the first paragraph. This must mean that the "payments" described in the preceding clauses are not all or entirely prohibited. Put another way, the language plainly calls for a distinction between payments that are used to secure a material advantage and those that are not. Thus, the ordinary, straightforward meaning of the material advantage clause is that payments that are used to secure a material advantage are prohibited subsidies, whereas payments that are not so used are not prohibited. Canada's submission contains no reading of the clause that would give the language its ordinary meaning and reach a different result.

(c) The Maxim *Expressio Unius Est Exclusio Alterius* Supports Brazil's Interpretation

20. Canada describes the *a contrario* rule as another way of referring to the maxim *expressio unius est exclusio alterius*, which means, in effect, that by stating one proposition in a text, the

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[18] Canada First Submission, para. 27.

[19] Korea – Definitive Safeguard Measure on Imports of Certain Dairy Products, WT/DS98/AB/R (12 January 2000), para. 80.

drafters necessarily excluded another proposition. Brazil agrees with Canada that the *a contrario* rule is related to the *expressio unius* maxim. However, Brazil disagrees with Canada that the maxim is unhelpful here. To the contrary, the *expressio unius* principle, as interpreted by the authorities relied upon by Canada, supports Brazil's construction of the first paragraph of item (k).

21. Put simply, the expressio *unius* maxim, in this case, means that by describing as prohibited subsidies payments "in so far as they are used to secure a material advantage," the drafters of the SCM Agreement necessarily intended that payments would *not* be prohibited export subsidies in so far as they are *not* used to secure a material advantage. The maxim is a "rule of both law and logic and applicable to the interpretation of treaties as well as municipal statutes and contracts."[20] In this instance, as a rule of law, the maxim corresponds with the principles of Article 31 of the Vienna Convention. The ordinary meaning of the language suggests that payments are prohibited only if they are used to secure a material advantage.

22. As a rule of logic, the maxim also supports Brazil's interpretation. Logically, had the drafters of the first paragraph intended to describe all "payments" as prohibited export subsidies, they simply would have ended the first paragraph right before the "in so far as" clause. The drafters did not so. Logically, therefore, they intended to qualify the description of payments that would be considered as prohibited subsidies so that *only* those payments described in the additional clause – those that are used to secure a material advantage – would be described as prohibited. Again logically, this means that the drafters intended that payments that did not fit that description – those that do not secure a material advantage – would not be proscribed.

23. Canada attempts to avoid this compelling logic by arguing that the maxim must be applied with caution. Canada quotes from a decision of an English court which stated that "the exclusio [i.e., the thing not expressly mentioned] is often the result of inadvertence or negligence, and the maxim ought not to be applied . . ."[21] This concern regarding the application, though no doubt valid, is not present here. It is impossible that the *exclusio* in this case was a result of inadvertence or negligence. To the contrary, the history of the first paragraph and the "material advantage" clause – the *expressio* in this case – makes clear that the clause was deliberately added to "restrict the definition of this type of export subsidy to instances where a 'material advantage' has been 'secured.'"[22]

24. The language that now comprises the first paragraph of item (k), *without* the material advantage clause, had its origins in rules adopted in 1958 by the Organization for European Economic Cooperation (the "OEEC"), the predecessor of the OECD, which prohibited:

> (g) The grant by governments (or special institutions controlled by governments) of export credits at rates below those which they have to pay in order to obtain the funds so employed;
>
> (h) The government bearing all or part of the costs incurred by exporters in obtaining credit.[23]

25. These provisions were included *verbatim* in a 1960 Report of a GATT Working Party on Subsidies as examples of export subsidies.[24] Subsequently, they provided the basis for the Illustrative List that eventually was included in the Tokyo Round Subsidies Code. It is significant, however, that

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[20] *United States v. Germany*, 7 R.I.A.A. 91, 111 (1924) (the *Life Insurance Claims* arbitration).
[21] Colquhoun v. Brooks, 21 QBD 52, 65.
[22] *Brazil – Export Financing Programme for Aircraft,*

in their first appearance in a GATT document, and for the next 18 years, these provisions contained

3. PROEX III Payments Are "Payments" within the Meaning of the First Paragraph of Item (k)

39. Canada argues that PROEX III payments are not payments within the meaning of item (k) first paragraph. Canada draws a distinction between *providing* export credits, and payment of all or part of the costs of *obtaining* export credits.[43] This distinction forms the basis of Canada's arguments that PROEX III interest rate support payments are not "payments" within the meaning of the first paragraph. As explained below, this distinction makes no sense in the context of the market for regional jet aircraft. Moreover, if PROEX payments do not fit the definition of "payments" contemplated by item (k), Canada fails to explain exactly what kind of payments in the export credit field the drafters of this provision had in mind.

40. The original Article 21.5 Panel stated that, "a payment by Brazil that allowed a Brazilian financial institution to provide export credits" could be permitted under the first paragraph of item (k) provided no benefit is conferred.[44] This would appear to contemplate that PROEX payments fell within the definition of the first paragraph, in that by enabling the Brazilian financial institution to *provide* export credits, it first had to pay the costs of *obtaining* the credits. This interpretation also would appear to be consistent with the ordinary meaning and purpose of the definition of "payments" in the first paragraph.[45] Canada has failed to provide any reasoned explanation why this interpretation is not appropriate.

41. The distinction between "obtaining" and "providing" credits fails for another reason. The first paragraph of item (k) refers, *inter alia*, to costs "incurred by exporters or financial institutions in obtaining credits." The language clearly contemplates that exporters and financial institutions "obtain" credits. But neither wants to "obtain" credits simply to hoard them. Both "provide" to export purchasers the credits they previously "obtain." That is the reason they are obtained. The fact that an exporter or a financial institution also provides credits does not mean that it does not obtain them at a cost.

42. The first sentence of item (k) first paragraph supports this conclusion. It deals with the grant by governments "of export credits at rates below those which they actually have to pay for *the funds so employed*." Just as the use of the term "export credits" in the first part of the paragraph justifies an interpretation of "credits" as meaning the same in the latter part, so also the reference to "the funds so employed" in the first part justifies an interpretation of the word "obtaining" in the second part as meaning "obtaining the funds [that are] so employed" when they are subsequently provided to export purchasers. This suggests that the language was intended to cover the provision of export credits to borrowers at a cost that is less than the borrower might otherwise have to pay. PROEX reduces the net interest rate to the borrower at a cost to the provider. The language of the first paragraph appears to have been designed to address precisely this type of programme.

43. Canada argues that Embraer itself does not provide export financing, and that non-Brazilian financial institutions sometimes do so. While both of these statements are factually correct, the legal conclusions reached by Canada do not follow. Canada's analysis fails totally to distinguish between situations in which the lender is a financial institution *outside* Brazil and situations in which the lender is a financial institution *inside* Brazil. Both in the original proceeding and in the Article 21.5 proceeding, Brazil carefully distinguished between these two situations, and offered very different legal justifications for each.

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[43] Canada First Submission, paras. 67-69.

[44] Original 21.5 Report, para. 6.44 .

[45] THE NEW SHORTER OXFORD ENGLISH DICTIONARY 2130 (1993) (A "payment is "a sum of money paid").

44. *When the lending institution is outside Brazil*, Embraer, the exporter, faces costs in obtaining for its customer a financial package that is competitive in the market. If it cannot obtain a competitive financial package for its customer, it would be forced to take other costly action such as paying for a commercially available loan guarantee at a high premium. *When the lender is inside Brazil,* it is the lender itself who must obtain the dollars on the market.[46] These separate justifications required separate analyses, a fact that Canada's arguments ignore. Moreover, while the question whether a payment is made to an institution inside or outside Brazil may have a bearing on the issue of material advantage, it has no bearing on the issue of payment. The payment is the same in either case.

45. Brazil risk is a genuine phenomenon that seriously handicaps financial institutions in Brazil in raising funds internationally, just as a similar risk handicaps comparable institutions in virtually all

be at or above the relevant CIRR.[51] Thus, PROEX III complies fully with the CIRR – the preferred

any advantage by providing equalization at the CIRR. Even if the market were to fluctuate slightly, Brazil does not secure a *material* advantage by providing equalization at this level. The ordinary market definition of "material" is "serious, important, of consequence."[57] Minor market deviations from the CIRR that are not "serious, important, of consequence" are not "material." The Appellate Body has noted that the term "material" cannot be read out of the language of the first paragraph.[58] Canada's analysis would do exactly that.

56. Finally, Canada states that the provisions of Resolution 002799, which it describes as providing for rates "in accordance with" the CIRR, do not necessarily prohibit PROEX III from supporting a minimum interest rate below the CIRR.[59] Brazil notes that the translation of Resolution 2799 requires interest rates "complying with" the CIRR.[60] Brazil reiterates that the minimum interest rate specified in PROEX III is the CIRR. This is the purpose of the Resolution. However, the CIRR is not necessarily the ceiling – Article 8, para. 2 of Resolution 002799 provides that the Committee on Export Credits is to use "as reference the financing terms practiced in the international market."[61] This provides additional assurance that PROEX III support will not secure a material advantage.

57. For these reasons, the Panel should conclude that PROEX III does not secure a material advantage in the field of export credit terms and that Brazil has therefore affirmatively shown that PROEX III is not a prohibited subsidy within the meaning of the first paragraph of item (k) of the SCM Agreement.

C. CANADA HAS FAILED TO SHOW THAT PROEX III DOES NOT QUALIFY FOR THE "SAFE HAVEN" OF THE SECOND PARAGRAPH OF ITEM (K)

58. In its First Submission of 16 March 2001, Brazil explained that PROEX III qualifies for the "safe haven" of the second paragraph of item (k) of the Illustrative List in Annex I of the SCM Agreement, and is therefore not a prohibited export subsidy within the meaning of the SCM Agreement. Brazil explained that PROEX III conformed to the minimum interest rate provision of the *Arrangement* – by requiring that all PROEX equalization comply with the CIRR – and also to the provisions governing the term and amount of financing – whether judged against the provisions of the 1992 *Arrangement* (as Brazil believes proper) or the provisions of the 1998 *Arrangement.*

59. As noted above, Canada does not in its First Submission address the issue whether PROEX III qualifies for the safe haven of the second paragraph. Instead, Canada addresses only the issues raised by item (k) first paragraph. However, the two paragraphs are not coterminous, and Brazil's arguments regarding the second paragraph are not undermined by Canada's arguments regarding the first paragraph.

60. The three points at issue under the first paragraph do not arise under the second paragraph. There is no need for an *a contrario* interpretation of the second paragraph, which states affirmatively that "if in practice a Member applies the interest rate provisions of the relevant undertaking, an export credit practice which is in conformity with those provisions shall not be considered an export subsidy prohibited by this Agreement." Accordingly, Canada's arguments regarding the *a contrario* issue are not relevant to the issue whether PROEX III qualifies for the safe haven of the second paragraph of item (k).

61. Similarly, the "payment" issue raised by Canada regarding the first paragraph of item (k) is irrelevant in the context of the second paragraph. Regardless of whether PROEX III meets the

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[57] The New Shorter Oxford Dictionary 1713-14 (1993).
[58] Appellate Body Report, para. 177.
[59] Canada First Submission, para. 71.
[60] First Submission of Brazil, para. 7, Exhibit Bra-1.
[61] Id.

definition of "payments" within the first paragraph, PROEX III is indisputably an "export credit practice" as contemplated by the second paragraph of item (k). As the Article 21.5 Panel in *Canada – Aircraft* stated, "we can conceive of no basis to consider any practice associated with export credits as *a priori* not constituting an 'export credit practice' in the sense of the second paragraph of item (k)."[62] It is not disputed that Brazil's practice of providing interest rate support is an "export credit practice" of the kind long practiced by various members of the OECD.[63]

62. Finally, the issue whether the PROEX III payments are used to "secure a material advantage in the field of export credit terms" does not arise under item (k) second paragraph. There the issue is not whether the PROEX interest rate support payments are used to secure a material advantage, but rather whether Brazil complies with the interest rates provisions of the *Arrangement.* Canada's arguments that the CIRR may not accurately reflect the market[64] are quite simply irrelevant to the issue whether PROEX III, by its terms, conforms with the interest rate provisions of the *Arrangement* and therefore qualifies for the safe haven of the second paragraph of item (k).

V. CONCLUSION

63. For all of the reasons given in Brazil's First Submission and in this Submission, the Panel should conclude that:

(a) Canada has not sustained its burden of proving that PROEX III is a subsidy within the meaning of Article I of the SCM Agreement;

(b) Alternatively, even if PROEX III were considered to be a subsidy, it complies with the interest rates provisions of the relevant *OECD Arrangement* and is, therefore, covered by the "safe haven" of item (k) second paragraph;

(c) Further, even if PROEX III were considered to be a subsidy, and even if it were not eligible for the safe haven of item (k) second paragraph, PROEX III is not used to secure a material advantage in the field of export credit terms within the meaning of item (k) first paragraph.

[62] Canada – Measures Affecting the Export of Civil Aircraft – Recourse by Brazil to Article 21.5 of the DSU, Report of the Panel, WT/DS70/RW (9 May 2000), para 5.81.

[63] Ray, *supra*, at pp. 22-24.

[64] The OECD members clearly intended that the CIRR would indeed reflect market rates. Members that are not participants in the *OECD* Arrangement, such as Brazil, have no control over these rates and should not be punished when they comply with the rates only to have OECD participant Members decide that the CIRR rates do not suit their purpose after all.

LIST OF EXHIBITS

BRA-10. Steve Cutts and Janet West, "The Arrangement on Export Credits," *The OECD Observer* No. 211, April/May 1998

BRA-11. JOHN E. RAY, MANAGING OFFICIAL EXPORT CREDITS – THE QUEST FOR A GLOBAL REGIME, Institute for International Economics (1995)

BRA-12. GARY CLYDE HUFBAUER AND JOANNA SHELTON ERB, SUBSIDIES IN INTERNATIONAL TRADE 70 (Washington, D.C., Institute for International Economics 1984)

BRA-13. General Agreement on Tariffs and Trade, Multilateral Trade Negotiations, Group "Non-Tariff Measures," Sub-Group "Subsidies and Countervailing Duties," SUBSIDIES/COUNTERVAILING MEASURES, Outline of an Arrangement, MTN/NTM/W/168, 10 July 1978

BRA-14. General Agreement on Tariffs and Trade, Multilateral Trade Negotiations, Group "Non-Tariff Measures," Sub-Group "Subsidies and Countervailing Duties," SUBSIDIES/COUNTERVAILING MEASURES, Outline of an Arrangement, MTN/NTM/W/210, 19 December 1978

ANNEX B-3

ORAL STATEMENT OF BRAZIL

(4 April 2001)

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is not Brazil's obligation to prove the negative, to prove that PROEX III does not confer a subsidy. Canada has failed to sustain its burden of proof on the question of benefit, and the efforts of the European Communities and the United States, as third parties, to support Canada on this question are not successful.

5. Canada's "proof" as to benefit consists of several descriptive statements about PROEX I and PROEX II, which are not relevant to this proceeding, and allegations concerning Brazil's development bank, Banco Nacional de Desenvolvimento Economico e Social ("BNDES"). We are somewhat confused by Canada's reference to BNDES, Mr. Chairman, and by the point Canada attempts to make. BNDES has never been within the terms of reference of this dispute. In any event, statements about PROEX I, PROEX II, or BNDES are not evidence establishing that PROEX III confers a benefit.

6. In the absence of evidence, Canada resorts to faulty logic. For example, at paragraph 12 of its Second Submission, Canada argues that "PROEX III, like its predecessor schemes, is constructed as a buy-down of interest rates that have already been freely negotiated by the recipients – Embraer's customers – in the marketplace." Canada then concludes that "*any* buy-down below those freely negotiated rates will *necessarily* result in net interest rates on terms more favourable than those available to Embraer's customers in the market."

7. It is misleading, if not inaccurate, to say that PROEX III is a buy-down of interest rates that have already been freely negotiated by the recipients in the market place. PROEX III is limited, on its face, to a maximum payment of 2.5 percent, with a minimum rate of the CIRR, and is, further, subject to being "compatible with [financing costs] practiced in the international market." PROEX is *not* a system, as Canada seems to suggest, whereby the customer negotiates for the most favorable rate, and then receives a "buy-down" of 2.5 percent. To the contrary, PROEX is part of the transaction itself – a transaction that is *limited* by the market, as reflected in the CIRR, a 10-year term, and 85 percent maximum financing, and by the requirement that the resulting transaction be compatible with the international market.

8. Thus, PROEX most certainly does *not* "*necessarily* result in net interest rates terms more favourable than those available to Embraer's customers *in the market*." Whether the resulting net interest rate terms are or are not more favourable than those a customer could obtain "in the market" is a question of fact. PROEX III does not provide for rates that are more favorable than those a customer could obtain "in the market." The theoretical possibility that more favourable terms could be offered in some future transaction is not evidence that they would be offered, and is not relevant to the question of what PROEX III, on its face, as a matter of law, provides.

9. The Panels in the *Canada – Aircraft* cases, for example, pointed out that the fact that Canada's export credit agency, the Export Development Corporation – "EDC" – *could* provide financing on a preferential basis, does not mean that it *would* do so. Those Panels also pointed out that the mere fact that Canada's Technology Partnerships Canada *could* provide a subsidy contingent on export, does not mean that it *would* do so. Likewise, the theoretical possibility that PROEX III *could* provide terms more favorable to a customer than could be obtained in the market does not mean that PROEX III *would* so provide.

10. Canada claims that financing being provided by BNDES – which, as I have already noted, is not and never has been within the terms of reference for this dispute – is being offered "in conjunction with PROEX III." There are several problems with this claim. First, it is simply irrelevant whether BNDES is involved in financing Brazilian aircraft transactions. The second is that Canada's "evidence" in support of its claim is a statement by a Bombardier employee reporting on what an airline official allegedly told the Bombardier employee that Embraer allegedly offered to the airline.

11. In law, this kind of evidence is what is referred to as "hearsay" – that is, it is the mere repetition of what someone claims to have heard another say. In this case, what Canada is offering is

"triple hearsay" – (1) Canada's statement of what a Bombardier employee said about (2) what an airline official said about (3) what Embraer said.

12. Now, Brazil is willing to acknowledge, Mr. Chairman, that just because evidence is hearsay, even triple hearsay, does not necessarily mean that it is always wrong. But Brazil does suggest that the possibility for error in such a lengthy transmission is high, particularly given the fact that an airline, in this situation, might be said to have an incentive to exaggerate in its statements to one potential vendor about what another potential vendor is offering.

13. Finally, there is an overriding reason why this evidence is not relevant. It is at most evidence of what an *Embraer sales person* said. The Government of Brazil cannot take responsibility for the alleged statements of Embraer sales persons.

14. Canada concludes its "evidence" on benefit with the statement, in paragraph 17, that "Canada demonstrated in its First Submission that the CIRR alone, divorced from the other terms and conditions of the OECD Arrangement such as the ten-year term limit and the limit on financing to 85 percent of the value of the contract, in no way reflects market realities. Brazil has not rebutted Canada's evidence and submissions on this point."

15. This is a rather surprising statement, Mr. Chairman. As I thought we made clear in our First Submission, PROEX III is not "divorced" from the 10-year term limit and the limit on financing to 85 percent of the value of the contract. PROEX III specifically includes these requirements.

16. Indeed, if another piece of Canada's hearsay evidence is to be believed, Brazil is financing considerably less than 85 percent of the value of the contract. Canada's Exhibit 27 is more triple

21. The arguments of the third parties do not advance Canada's case. The European Communities, at paragraph 12 of their submission, repeat Canada's claim that PROEX is used to reduce a commercially negotiated contract by 2.5 percent. I have already pointed out why this reasoning is wrong. At paragraph 14, the European Communities claim that the CIRR is a rate that would be available to borrowers only in the presence of a guarantee or other security. But all transactions involving aircraft are secured – by the aircraft themselves, if not by other means, such as residual value guarantees.

22. The United States, at paragraph 11, "wishes to note only that interest rate support at or above CIRR does not, *ipso facto*, mean no benefit is conferred." This formulation reverses the issue. It is

that an existing treaty *may* be subject to the terms of a later treaty, but only when the terms of the existing treaty "specify" that this is the case.

29. Further, as part of the context, Brazil referred to the fact that, in the case of Members that incorporate the WTO Agreements into their domestic law, serious constitutional questions would be raised if later versions of the *Arrangement* were included in the second paragraph of item (k). This would amount to a *carte blanche* to non-citizens to change the domestic law of these Members. It is not only Brazil that would be in this position, Mr. Chairman. A substantial number of Members incorporate WTO Agreements directly into their domestic law.

30. Third, Brazil noted the object and purpose of the SCM Agreement. While the Agreement does not, on its face, contain a statement of its object and purpose, there can be little dispute that these include establishing disciplines for the conduct of Members in providing subsidies – disciplines that are clear, transparent, and fair.

31. There is nothing clear, transparent or fair about an interpretation of the second paragraph that would permit a small group of developed countries to change the terms of the SCM Agreement anytime they choose, in whatever way they choose. Certainly there is nothing fair about an interpretation that, for example, would allow Canada and the other participants in the *Arrangement* to provide that interest rate support may not be used for regional aircraft. Canada, however, seems to think there is nothing wrong with this.

32. This is not a theoretical risk, Mr. Chairman. I will have more to say about the question of spare parts shortly, but for now let me just note that the handling of spare parts by the participants in the *Arrangement* is a clear example of how Canada would have the system work. Under the 1992 version of the *Arrangement*, its spare parts provisions did not apply to regional aircraft. Under the 1998 version, they do apply – and Canada is citing those provisions as grounds for excluding Brazil from the safe haven of the second paragraph.

33. The sequence of events in this dispute and in the change in the terms of the *Arrangement* is very significant. Let's assume, for purposes of analysis of these events, that the spare parts provision of the *Arrangement* is an interest rate provision, and that PROEX III does not in practice apply that provision – (as I will explain later, Brazil does not agree with either of these assumptions).

34. In 1995, when the SCM Agreement was adopted, Brazil would not have had to apply the spare parts provision in order to be in compliance with the second paragraph, since the provision explicitly did not apply to regional aircraft in the version of the *Arrangement* in effect at that time. In 1996, when Canada began this dispute with its request for consultations, Brazil still would not have had to apply the provision, since the 1992 version remained in effect.

35.

into force. Once again, the drafters could have said "will be," or "may be" adopted. But they said "has been," "haya sido," "a été" adopted.

45. While the *Canada-Aircraft* Panel did discuss the 1998 version of the *Arrangement*, the question of which version was relevant was never at issue in that proceeding. The parties neither briefed nor argued the question. It was not discussed by the parties in their meetings with the Panel. Consequently, that Panel's assumptions, which are not binding on this Panel, were clearly for the purpose of addressing the issue before it. That issue is not the issue here.

46. This ends Canada's rebuttal to Brazil's arguments. Canada did not address Brazil's arguments regarding the context of the second paragraph, particularly in light of the amendment provisions of the WTO Agreement. Canada did not address the object and purpose of the SCM Agreement, which, at a minimum, includes clarity, transparency, and fairness. Canada did not address Brazil's argument under Article 32(b) of the Vienna Convention that an interpretation of the second paragraph that applies the 1998 and all later versions of the *Arrangement* leads to a result that is manifestly absurd and unreasonable.

47. Even assuming that the interpretation advocated by Canada is a possible interpretation of the "has been adopted" clause of item (k) second paragraph, there can be no dispute that, at the very least, the interpretation advocated by Brazil also is a possible interpretation of that clause. In such circumstances, the Panel should adopt the interpretation that avoids an absurd or unreasonable result. There is nothing in the text of item (k) that unequivocally specifies that WTO Members have given a few countries the right to *perpetually* legislate on behalf of the overwhelming majority of the membership.

48. The third parties do not salvage the situation for Canada. The United States repeats Canada's moving goal post argument, that "has been" refers to the time when an export credit is granted. The United States then goes on to say, at paragraph 7, that Brazil's interpretation is illogical "since it would suggest that a Member could grant export credits that are not in compliance with the most recent version of the *Arrangement*, and yet still benefit from the safe harbour in item (k)."

49. Brazil sees nothing illogical at all in this, Mr. Chairman. There is nothing illogical in an interpretation of the second paragraph to mean that all WTO Members are bound by the version of the *Arrangement* in effect at the time when it was incorporated into the SCM Agreement. If other Members – whether 23 of them or only the original 12 – wish to agree to stricter standards among themselves, then by all means they are free to do so. What is illogical, Mr. Chairman, is an interpretation of the second paragraph that would permit 12 or 23 OECD participants to change the terms of the SCM Agreement for all of the WTO Members.

50. The United States addresses Brazil's fairness point by referring to Article 27 and its temporary exemption from Article 3's prohibition for developing countries. Article 27 is hardly relevant to the interpretation of the second paragraph of item (k). Moreover, as the Panel knows, Article 27 has strict conditions for the exemption. Further, the exemption expires in two years, as the United States admits. Article 27 does not justify permitting 12 or 23 OECD participants to make rules for the entire WTO.

51. The United States further argues that the drafters of the Tokyo Round Subsidies Code, referring to the *Arrangement* as of 1 January 1979, and then to a "successor undertaking," clearly referred to a successor undertaking adopted after the Tokyo Round. Following the very same logic, however, the drafters of the Uruguay Round Subsidies Agreement should have referred to the *Arrangement* "as of 1 January 1995" and then to a "successor undertaking." They did not do that. Thus, what may have been clear and explicit in 1980 (and Brazil does not agree that it was) is at best unclear and ambiguous in 1995. In fact, the Tokyo Round Code came into effect on 1 January 1980, a full year after the 1 January 1979 effective date of the *Arrangement*. The reference in item (k) of the

Tokyo Round Code to a "successor undertaking," in Brazil's view, is a reference to any possible further action within the OECD that might have been taken during that year.

52. The European Communities repeats the arguments raised by Canada and the US, and then adds two of its own. First, the EC argues that a change in the *Arrangement* does not amend the SCM Agreement since the text of the second paragraph itself is not changed by action in the OECD. This argument ignores the fact that, by virtue of the second paragraph, the *Arrangement* becomes a WTO text, just as the major intellectual property conventions are WTO text (in their 1995 versions only), and just as the Lomé Convention was found to be a WTO text by the Panel in *Bananas* because it was incorporated by reference into the WTO by means of a waiver. A change in these documents is a change in the relevant WTO text. Indeed, the EC concedes as much. At paragraph 30, the EC observes, "It may appear strange that the WTO Members should have agreed to apply a *text* that could only be changed by a small number of them." That it is a *text* that applies to the WTO that is being changed cannot be doubted.

53. I have already given a concrete example of how, under Canada' s theory, WTO obligations could be changed by a change in the *Arrangement* – the example of the spare parts provisions, which indisputably did not apply to regional aircraft in the version in existence on 1 January 1995, and which undisputedly do apply to regional aircraft in the current version. It is difficult to imagine a clearer example of an effective change in a WTO text. The fact that a text was adopted by the WTO, rather than being written by it, does not mean that it is not a WTO text.

54. The second argument made by the EC that differs from the arguments made by Canada and the US concerns other parts of the WTO Agreements that may authorize action by other international organizations. The EC points to Article XXI of GATT 1994, which allows Members to take action in pursuance of their obligations under the United Nations Charter for the maintenance of international peace and security. It also points to the TBT and SPS Agreements, which require Members to take international standards into account in setting their own standards. For that matter, the EC could have pointed to Articles XIV and XV of GATT 1994, which make certain decisions of the International Monetary Fund applicable to WTO Members.

55. These are all true and, equally, these are all irrelevant for the issue before you concerning the second paragraph of item (k).

56. Brazil has never disputed that international organizations *may* specify that the provisions or decisions of other treaties or organizations shall apply. The question is whether, in a particular instance, this has been done. In the case of giving overriding authority to the United Nations on matters of peace and security there can be little argument. GATT 1994 explicitly does so specify. It is worth pointing out, as well, that all Members of the WTO are eligible for membership in the UN, and most, if not all of them, are members. Similarly, GATT 1994 gives certain powers to the International Monetary Fund. These powers relate to balance of payments issues and were included in GATT 1947 in the context of the entire Bretton Woods system, which sought to combine freer trade with fixed exchange rates. There was an obvious need for cooperation among the organizations, as fixed exchange rates and import quotas established to protect those rates, could have had an obvious impact on the trading system. Again, it is worth pointing out that all Members of the WTO are eligible for membership in the IMF, and most, if not all of them, are members.

57. With regard to the TBT and SPS Agreements, the EC greatly overstates its case. It is true, as the EC states, that provisions of both Agreements call upon Members to base their standards on international standards. But it is also true that each of those provisions contains exceptions; Members are not required to follow international standards in order to comply with their WTO obligations. It is further true that other paragraphs of the same articles of those Agreements, cited by the EC, call upon WTO Members to play a full part in the international standard-setting organizations, which are open to membership by all nations. There are no comparable exceptions in the second paragraph of

item (k), and all WTO Members most certainly are not called upon by that paragraph to play a full part in the OECD. Most WTO Members are not eligible to join the OECD and, even if eligible, any effort to join would be rejected.

58. Finally, the EC disagrees with Brazil's argument that changes in the *Arrangement* occur in a non-transparent manner. "The current version of the *OECD Arrangement* is publicly disclosed by the OECD, " the EC writes at paragraph 29, "and is available on the OECD web site." In a footnote to this statement, the EC is good enough to supply the internet address of the OECD.

59. Mr. Chairman, it is Brazil's position that Members of the WTO should not be required to check the web site of the OECD to learn what their WTO obligations are. An interpretation of the second paragraph of item (k) that results in such a requirement would, in the view of Brazil, be a result that is manifestly absurd and unreasonable within the meaning of Article 32(b) of the Vienna Convention. That interpretation should be rejected.

C. PROEX III COMPLIES WITH THE INTEREST RATES PROVISIONS OF BOTH THE 1992 AND 1998 VERSIONS OF THE *ARRANGEMENT*

60. Mr. Chairman, I will not take the time to repeat here the points made in Brazil's First Submission that demonstrate that Brazil is in compliance with the interest rates provisions of both the 1992 and the 1998 versions of the *Arrangement.* Instead, I will address only the points raised by Canada regarding Brazil's alleged failure to apply those provisions, in practice, through PROEX III. The third parties, I note, did not address the specifics of Brazil's argument concerning its application of the interest rates provisions, but rather addressed the broader question of what, in fact, are the interest rates provisions – a subject Brazil addressed in its First Submission.

61. At paragraph 50 of its Second Submission, Canada claims that PROEX III does not conform to what it calls two of the key requirements of both the 1998 and 1992 versions of the *Arrangement.* These are the requirements that support be limited to terms of 10 years and cover no more than 85 percent of the value of the goods financed.

62. But PROEX III, on its face, complies with these requirements. As Brazil noted in paragraph 9 of its First Submission, and as set out in Brazil's Exhibit 3, Directive 374 limits PROEX interest rate equalization to 85 percent of the value of the transaction, and establishes a maximum financing term of 10 years for regional jet aircraft. Thus, even by Canada's definition, Brazil in practice applies the interest rates provisions of the 1992 version of the *Arrangement* – and also applies at least these two provisions of the 1998 version as well.

63. The only other specific provisions of the 1998 version cited by Canada as not being addressed by PROEX III are Article 13 regarding repayment of principal and Article 29(a)-(c) of Annex III regarding spare parts. Let me address each of these in turn.

64. Article 13 of the *Arrangement* is entitled "Repayment of Principal." It does not even deal with interest – it deals only with principal. Even the *Canada-Aircraft* Panel, which took, in our opinion, an overly-broad view of the term "interest rates provisions" did not include Article 13 among them. Very plainly, Article 13 is not an interest rate provision.

65. The *Canada-Aircraft* Panel did identify Article 29(a)-(c) as among the interest rates provisions of the *Arrangement.* Brazil disagrees in part. Only the first sentence of Article 29(a) deals with interest rates, providing that the financing of spare parts "when contemplated as part of the original aircraft order may be on the same terms as for the aircraft." Brazil complies with this provision. To the minimal extent that spare parts are part of an Embraer order, PROEX III provides that they should be financed on the same terms as the aircraft – at the CIRR, with a maximum of 85 percent financing, for 10 years.

customers. This interpretation is supported by the structure and logic of the first paragraph of item (k), which addresses two kinds of subsidies. The first kind of subsidy is the grant by a government itself of credits below its own cost of funds. The relevant issue here is the cost to the government in obtaining the funds *it* provides. The second kind of subsidy is governmental assistance to defray all or part of the costs incurred by exporters or financial institutions in obtaining the funds *they* provide. In both situations, funds provided are first obtained. In fact, the parenthetical clause in the first paragraph, describing the proper measure of the government's cost in obtaining funds is a description of the costs incurred by exporters or financial institutions in obtaining credits that PROEX is intended to address. This clause refers to costs that actually are paid or would have to be paid "on international capital markets in order to obtain funds of the same maturity … denominated in the same currency as the export credit." Almost all PROEX payments are made to banks in Brazil that incur costs in obtaining dollars on international capital markets.

75. The United States supports Brazil's position on the definition of "payment" in the first paragraph of item (k). The United States points out that the term covers not only direct payments, but also payments that reduce the risk incurred by the exporter or the financial institution. Therefore, in the view of the United States, PROEX interest rate support is a "payment" under the first paragraph of item (k). Brazil agrees. In addition, the United States correctly observes that the first paragraph of item (k) should be interpreted within the context of the Agreement and general export credit practice. Interest rate support payments, like PROEX, reduce the risk incurred by exporters or financial institutions, just as such practices as insurance and guarantees reduce the risk.

76. In Brazil's view, one way to look at the payment issue is to go back to the original 1958 language of the OEEC, which is set out in paragraph 24 of its Second Submission: "The government *bearing all or part of the costs* incurred by exporters in obtaining credits."

77. This was the initial description of an export subsidy, that eventually found its way into item (k) first paragraph. One of the 1979 additions to this language was the inclusion of "financial institutions" as well as exporters as the target recipients of what were deemed export subsides. This extended the original 1958 prohibition, which covered only suppliers' credits, to buyers' credits as well. Thus, as modified by this single change, the 1958 example of an export subsidy was: "The government *bearing all or part of the costs* incurred by exporters [or financial institutions] in obtaining credits."

78. The Panel should ask itself, if this language appeared, as it is, without any qualification, in Annex I to the SCM Agreement, would it apply to PROEX III? In Brazil's view, there can be little doubt that it would. With PROEX III, the Government of Brazil, in making PROEX payments, *bears all or part of the costs* incurred by exporters or financial institutions in obtaining credit. If this were all that was encompassed by the first paragraph of item (k), PROEX III would be prohibited.

79. But item (k) says more. It says, "in so far as they are used to secure a material advantage in the field of export credit terms." When this language is given full and complete effect by an *a contrario* interpretation, it leaves unresolved only the third point that Brazil must establish: material advantage.

80. In its August 1999 Report, at paragraph 181, the Appellate Body concluded that interest rates at or above the CIRR do not confer a material advantage. In paragraph 6.87 of its May 2000 Report in the original Article 21.5 Review, the Panel found that the Appellate Body did not intend to duplicate, in the first paragraph, all of the elements that were necessary to secure the safe haven of the second paragraph. PROEX III employs the CIRR as a floor, a floor that may be elevated, as necessary, to be compatible with the international market. Thus, under the test established by the Appellate Body and the Article 21.5 Panel, PROEX III is not used to secure a material advantage.

ANNEX B-4

CLOSING STATEMENT OF BRAZIL

(5 April 2001)

1. [Minister Patriota] Good afternoon, Mr. Chairman. I would like to thank the Panel for the opportunity to present these closing remarks this afternoon. There are just two points I would like to make before asking my colleague Mr. Azevedo to address some additional points.

2. Mr. Chairman, it was a difficult job to change PROEX III. As you heard this morning from Mr. Azevedo, who was at the meetings in Brasilia and was involved in the process, there was opposition in Brazil to making the changes. Indeed, I would go so far as to say that there was bitterness and anger in some quarters. Some people did not want to make the necessary changes in response to the previous findings. Nevertheless, we got the job done and what you have before you is PROEX III. This is what you must review.

3. I would also like to address an issue that is very important to Brazil. This is the issue of what version of the *OECD Arrangement* applies. We believe that the Panel should apply the 1992 version instead of the 1998 version. As we explained in our oral statement, we do not think that the Panel should prefer an interpretation of the SCM Agreement that would give a small number of members of the OECD the perpetual power to change the rules for the remaining Members of the WTO. The Panel should not follow an interpretation that would lead to such an unfair result. You know our views on this, and I would sum up by simply repeating a sentence from paragraph 47 of our oral statement yesterday: there is nothing in the text of item (k) that unequivocally specifies that WTO Members have given a few countries the right to perpetually legislate on behalf of the overwhelming majority of the membership. This is of particular concern if we are to bear in mind that these few countries would be acting within the framework of an organization, the OECD, which is not open to universal accession.

4. I would now ask Mr. Azevedo to make the remainder of Brazil's points.

5. [Counselor Azevedo] Thank you. I would first like to address an issue that we have not

sales person might offer to a customer. Brazil is only responsible for interest rates support approved under PROEX III. A sales person might offer terms that would not be subsequently approved by the Committee. An offer in itself, even if such an offer were made by a sales person, is not in itself evidence of breach of Brazil's obligations under the SCM Agreement.

14. In conclusion, Mr. Chairman, Brazil would like once again to emphasize that PROEX III conforms to Brazil's WTO obligations. PROEX III confers no benefit and, therefore, is not a subsidy. Alternatively, through PROEX III, Brazil in practice applies the interest rates provisions of the *OECD Arrangement* and, therefore, PROEX III is covered by the safe haven of the second paragraph of item (k) of the Illustrative List. Finally, in case the Panel disagrees with both of these arguments, PROEX III is a payment under the first paragraph of item (k) which is not used to provide material advantage and, consequently, is not a prohibited subsidy.

ANNEX B-5

PROEX II "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" does not accurately reflect the process, particularly with respect to PROEX III. The process of negotiating a sale and obtaining PROEX support is not a linear process, and does not result in a commercially-negotiated interest rate that is then further reduced by PROEX support. Put another way, the parties do not negotiate a commercial rate and then use that as the starting point in applying for PROEX support, which, if granted, would *further* reduce the commercially negotiated rate.

To the contrary, the negotiations are a complex process that involve several parties – including at a minimum the seller, the lender, and the buyer. There may be equity investors, guarantors, insurers and other parties also involved in the transaction. Frequently, the buyer also may be negotiating with several potential sellers and other lenders. These negotiations are controlled by the prevailing commercial rates in the market place. However, the possibility of PROEX involvement in the transaction does not reduce the net interest rate below what would otherwise be available in the marketplace; it simply places the rates available to purchasers of Brazilian aircraft at the same level as rates available for other regional jet aircraft from other vendors with their financial institutions.

This may arise in three situations. In the first, a buyer – assume a Chinese buyer – may be quoted an interest rate of eight percent (assume this is at/above the CIRR) by an international financial institution, such as Chase Manhattan or Citibank, to purchase Brazilian aircraft. A Brazilian bank may not be able to offer eight percent without PROEX support. In this case, PROEX may enable the Brazilian bank to provide the Chinese buyer the same terms as are available for that transaction in the international marketplace (*i.e.*, Chase Manhattan or Citibank) but with the added convenience of dealing with a bank with whom the seller is familiar, and a bank that is more familiar with transactions of that kind. In financial terms, however, PROEX would not place the buyer in any better situation or give it any better terms for the transaction than are available in the international marketplace.

In the second situation, the Chinese buyer may be offered eight percent terms by an international financial institution (again, assume this is at/above the CIRR) to finance a purchase of Brazilian aircraft. The Chinese buyer, however, would prefer to finance the transaction through a Chinese bank. The Chinese bank, however, is able to offer credit only at 10 percent. In this case, PROEX support may enable the Chinese bank to provide credit at eight percent and thereby facilitate the buyer's preference for its own bank. Again, however, PROEX would not place the buyer in any better situation or give it any better terms for the transaction than are available in the international marketplace.

In the third situation, assume that an airline is quoted a rate of eight percent for a purchase of regional aircraft by an international financial institution (assume also that this rate is at the CIRR). Brazil's manufacturer, Embraer, may want to compete for the sale and offer the same financing package. However, a Brazilian bank may not be able to provide financing at eight percent because of its higher cost of dollars, but rather might quote a rate of nine percent. In those circumstances, Embraer may apply for PROEX support to enable it to offer financing at the eight percent rate. Again, this would enable Embraer to offer terms that are equal to, though not more favourable than, the terms that are available to the borrower in the international marketplace.

Accordingly, in each of these three situations, the first Article 21.5 Panel's conclusion that PROEX reduces a previously-negotiated rate below the commercial rate does not reflect how the market operates and how PROEX becomes involved in transactions.

Brazil's statement that PROEX would always "be more favorable to the purchaser than the terms it could obtain on its own, otherwise the purchaser would have no interest in PROEX" must be read in the context of the examples given above. If PROEX were not involved in the transaction, the purchaser would be offered a financing package at 9 percent by the Brazilian bank. In that case, the

purchaser would likely take the financing package offered by the competitor rather than the PROEX-supported package. However, the PROEX-support would still not result in a net interest rate that is lower than either the CIRR or the terms that might otherwise be available in the marketplace.

Thus, Brazil does indeed contest that PROEX III payments would allow a purchaser to "obtain financing on terms more favorable than those otherwise available to *that purchaser* in respect of the *particular transaction* in the *commercial* marketplace." While PROEX III payments may allow the purchaser a broader range of financing options, the rates offered with PROEX support would *not* allow the purchaser to obtain regional aircraft at terms more favorable than would be available through other financial institutions in the commercial marketplace. The requirement that the

Q4. Is Brazil through its benefit arguments suggesting that in some cases financial institutions receiving PROEX III payments receive the payments without in any way improving the terms and conditions of the financing in respect of which PROEX III payments are made, i.e., that PROEX III payments are in some cases exclusively a subsidy to a financial institution? If so, and given that PROEX III payments may be provided where financing is provided by non-Brazilian banks, is Brazil suggesting that PROEX III is a subsidy for foreign banks?

As explained in the answer to question 2 above, PROEX III payments would enable Embraer to provide a net interest rate at the rates prevailing in the market place. This does not enable the seller to provide financing at terms more favorable than are otherwise available in the marketplace. However, it must be borne in mind that in the international aviation market, it is important that manufacturers are in a position to offer competitive financing at prevailing market rates. No aircraft manufacturer in the world tells airlines, "This is the price. Pay cash, or go borrow the cash from a bank." It is the custom in the trade, established long before Brazil began producing aircraft, for the manufacturers to have available a financing package for their sales, and these packages generally include some form of official government support for export credits.

Other manufacturers in other countries all have export credit support available – Canada through EDC, the United States through Eximbank. PROEX payments enable Embraer to avoid a competitive disadvantage in the marketplace by enabling it to offer financing at the CIRR and market rates. To the extent that PROEX III results in one bank rather than another providing the financing for a particular transaction, then it is the case that the bank profits or benefits from the PROEX support. This applies even where the bank is not a Brazilian bank, but is in another country, particularly a developing country. PROEX III support enables that bank to participate *at international market rates* in a financing transaction in which it would not otherwise be able to participate.

Q5. Is the Committee on Export Credits required to approve operations meeting the eligibility criteria set forth in BCB Resolution 2799 and Directive 374 and the National Treasury thus required to provide equalisation (i.e. is there a conditional entitlement to PROEX III support)? Or does the Committee retain discretion regarding whether or not PROEX III support is provided even where the eligibility criteria are met?

The Committee on Export Credits is not required to approve interest rate support financing even in the case of transactions where all the eligibility criteria provided by PROEX III are met. There is nothing in PROEX III that imposes on the Committee an obligation automatically to approve the granting of interest rate support once the Committee establishes that the eligibility criteria of PROEX III are met. The Committee thus retains discretion regarding whether or not PROEX III support is provided.

Article 1 of BCB Resolution 002799, for example, states that " … the National Treasury *may* provide to the financing or re-financing agency, as the case may be, equalization enough to render financing costs compatible with those practiced in the international market." (Emphasis ours.) Further, Article 2 of Resolution 002799 states: "Equalization *may* be granted when financing the importer, for cash payments to the exporter established in Brazil, as well as when re-financing granted to the latter." Resolution 002799 therefore imposes no obligation on the Committee to provide interest rate support even when all the eligibility criteria are met. The Committee must comply with certain mandatory requirements (e.g., the CIRR, 85 percent of the value of the sale, 10 year period of financing) but retains the authority – subject to the terms of the esolution 002799 stah5 TD -0vt1.25 Tf 0P

Q6. Is there a requirement, under Brazilian internal law, for the executive branch of the government to interpret provisions of internal law and exercise discretion conferred on it under internal law in such a way as to conform to Brazil's WTO obligations? If so, please explain and submit evidence.

The Congress of Brazil has the power to ratify treaties signed by the Executive. When the Congress does so, it normally adopts legislation incorporating the treaty's text into Brazilian law. However, treaties may not have direct effect in Brazil unless, in addition to the legislation incorporating the treaty, the Executive also issues regulations giving internal effect to the treaty. The WTO Agreements have been incorporated and implemented into the domestic law of Brazil in this manner.

Because Brazil's WTO obligations have been implemented and have become part of Brazil's domestic law, the executive branch must comply with those obligations as it does in the case of any other obligations imposed on it by any other provision of Brazil's domestic law. If other provisions of Brazil's domestic law *allow* the Executive to act in a way that may be inconsistent with its WTO obligations, the potential conflict would be resolved in favor of consistency with Brazil's WTO obligations. The Executive, even if permitted to act in a manner inconsistent with the WTO by other provisions of Brazil's domestic law, would still *have the duty* under domestic law to comply with its WTO obligations because the WTO Agreements have been implemented in Brazil' s domestic law. The only situation where a conflict would arise is if another provision of Brazil's domestic law *requires* the Executive to act in a manner inconsistent with Brazil's WTO obligations. In such a case, there would be a conflict between one provision of Brazil's domestic law and another provision of Brazil's domestic law. This is *not* the case with PROEX III. There is nothing in PROEX III that *requires* Brazil's executive branch to act in a manner inconsistent with Brazil's WTO obligations. In applying PROEX III, the executive branch remains bound by Brazil's WTO obligations as implemented in Brazil's domestic law.

Q7.

Brazil responded to these arguments by pointing out that what Canada had done was insufficient. First, Brazil argued that Canada could not simply state that it had brought Canada Account in compliance only because there had been no new transactions. Second, Brazil argued that the "Policy Guideline" referred neither to the "interest rates provisions" of the *OECD Arrangement* nor to conformity with the second paragraph of item (k). It only stated an intention to comply with the *Arrangement* in its entirety, without any indication of the specific provisions with which it intended to comply[4] Brazil suggested that Canada should specify how it intended to comply with the interest rates provisions of the *Arrangement* and the particular interest rates provisions of the *Arrangement* with which it intended to comply[5] Brazil suggested that "[t]he minimum burden accorded to Canada must be to explain with some precision what 'comply with the OECD Arrangement' will mean.[6] Instead, Canada issued a one sentence "Policy Guideline" that merely suggested that under Canada Account prohibited export subsidies might not be granted. Under the Guideline, for example, Canada would have been free to utilize the "matching" provisions of the Arrangement. The Panel had found that these were not "interest rates provisions.[7]

PROEX III does considerably more than did Canada's implementation measures with respect to Canada Account and meets the standard proffered by Brazil, as described above. PROEX III is not a blanket statement that the programme complies with the *Arrangement.* PROEX III contains specific requirements that are consistent with the specific criteria set out in the interest rates and other relevant provisions of the *Arrangement* (e.g., the CIRR as a floor, financing up to 85 percent of the export value of a sale, financing for a period of up to 10 years). PROEX III imposes on the Committee specific eligibility criteria that meet or exceed the disciplines contained in the interest rates provisions of the *Arrangement.* Therefore, PROEX III does ensure that financing under its terms qualifies for the safe haven of the second paragraph of item (k).

Brazil also notes that the Appellate Body in *Canada – Aircraft* Article 21.5 proceedings found that "the words 'ensure' and 'future,' if taken too literally, might be read to mean that the Panel was seeking a strict guarantee or absolute assurance" as to the future application of the revised programme. The Appellate Body concluded that "[a] standard …, if so read, would … be very difficult, if not impossible, to satisfy since no one can predict how unknown administrators would apply, in the unknowable future, even the most conscientiously crafted compliance measure.[8] Brazil can thus do no more than adopt an implementation measure that specifically addresses the way in which it will, as a matter of law, comply with its WTO obligations – which is exactly what PROEX III does.

Q8. Brazil argues that "the maximum percentage allowed under PROEX III for the purpose of interest rate equalisation is 85 per cent of the export value of the sale" (Brazil's first submission, para. 43). Is it Brazil's position that PROEX III would not *allow* Brazil to exceed this maximum percentage in respect of regional aircraft? If so, why? When responding to this question, please specifically address:

(a) Article 5 of Directive 374;

(b) Article 8 of Directive 374;

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[4] *Id*., Annex 1-2 (Brazil Rebuttal Submission), para. 69.
[5] *Id*., para. 72.
[6] *Id*., para. 76.
[7] *Id*., paras. 5.125, 5.126, 5.132-5.134, and 5.147(d) and (f).
[8] *Canada – Measures Affecting the Export of Civilian Aircraft*, Recourse by Brazil to Article 21.5 of the DSU, Report of the Appellate Body, WT/DS70/AB/RW, 21 July 2000, para. 38.

(c) the statements reported by Canada in paragraph 11 of its first written submission and paragraphs 20-26 of its rebuttal submission.

(a) Brazil's position is indeed that PROEX III would not allow Brazil to exceed the maximum percentage for the purpose of interest rate equalization – 85 percent of the export value of the sale – with one possible exception. The rule is contained in Article 5 of Directive 374. Article 5 of Directive 374 prohibits interest rate equalization for more than 85 percent of the export value of the sale. The exception is contained in Article 8, para. 2 of BCB Resolution 002799, which allows departure from the specific eligibility criteria in PROEX III only when interest rate support is provided on terms consistent with the international market. Thus, if the Committee is satisfied by the applicant and its own research that interest rate equalization based on more than 85 percent of the export value of the sale would nonetheless be consistent with the terms prevailing in the international market, the Committee could (but would have no obligation to) provide interest rate support on the same terms as those available in the international market. In that instance, PROEX III would not confer a benefit, since it would provide support consistent with that available to the recipient in the market.

(b) Article 8 of Directive 374 does not allow Brazil to exceed the maximum percentage of 85 percent of the export value of the sale. This Article actually applies to requests of PROEX support that concern products that are not included in the Annex, or whose commercialisation in the international market require terms that exceed those set out in the programme. For example, the repayment term practiced in the international market could exceed the one stipulated in the Annex for that particular product. Article 8 ensures that the Secretaria de Comércio Exterior (SECEX) is aware of such situations with a view to reassess the operation of the programme in light of these circumstances. SECEX has no authority to approve the requests that do not conform to the basic guidelines of the programme. Such authority is vested on the Comitê de Crédito

Government about revising PROEX and of some public comments about Brazil's negotiations with Canada. They do not provide evidence of what PROEX III *actually requires*. This evidence is provided by the documents constituting PROEX III. Brazil has submitted those documents to the Panel. There is no better evidence about what PROEX III is and what PROEX III requires than the evidence contained in the PROEX III documents themselves.

Finally, Canada grossly misstates and misinterprets the positions and views expressed by Brazil during their negotiations. Canada states that Brazil publicly insisted that it would not abide by the provisions of the *OECD Arrangement* and that, during the negotiations, Brazil refused to consider adjusting PROEX to the interest rates provisions of the *Arrangement.* Canada ignores the fact that Brazil consistently has adhered to the view that the second paragraph of item (k) does not require

provision obviously applies to products with repayment terms under 96 months in the Annex. This is not the case for regional aircraft.

Article 4 deals with exports that involve more than one product and the application of the methodologies set out in items (a), (b), and paragraph 1 could not mathematically result in repayment terms longer than the 10 year maximum.

(b) See response to Question 8(c) above.

(c) The basis for Brazil's assertion that the maximum length of the financing term is 10 years is the specific requirement to that effect in Directive 374, and the requirement of Article 1.1 of BCB Resolution 002799 that interest rate equalization must be provided in compliance with the CIRR. As

aircraft. PROEX III is consistent with this in that the Annex to Directive 374 establishes a maximum repayment term of 10 years for regional jet aircraft.

Article 13 of the *Arrangement* calls for repayment of principle in regular instalments not less than six months in frequency. Similarly, Article 14 of the *Arrangement* calls for the payment of interest on a six-monthly basis. Article 4 of Resolution 2799 conforms with these requirements in that it provides for calculation of the amounts due for equalization purposes on a six-month basis and calls for the issuance of NTN-I bonds on a six-monthly basis.

Articles 16 and 17 govern the calculation of the CIRR. Resolution 2799 provides that the net interest rate for a PROEX-supported transaction may not be below the CIRR. Since Brazil is not a Participant in the *Arrangement* , however, Brazil does not play any role in calculating the CIRR and therefore PROEX III does not contain parallel provisions to Articles 16 and 17 governing how the CIRR is to be calculated.

Articles 18 through 24 of the *Arrangement* govern cosmetic interest rates and minimum premiums. These provisions do not apply to interest rate support and, therefore, are not relevant to PROEX III.

Article 25 of the *Arrangement*

Article 29 of the Annex provides for the financing of spare parts and engines. Brazil has stated its views on the applicability of Article 29(a) to PROEX in its First Submission (at paragraphs 59-61) and in its oral statement (at paragraphs 33-35). Articles 29(b) and (c) establish repayment terms of five years for spare engines and two years for other spare parts when not ordered with the new aircraft. Brazil notes that it does not manufacture engines and therefore does not sell engines separately from the aircraft. In any event, PROEX III conforms with these provisions to the extent that it establishes (in the Annex to Directive 374) that the maximum financing term for parts of aircraft shall be limited to five years (NCM Heading 8803) and one year (NCM Heading 8803.90). While the classification of goods is not entirely clear from the schedules, these classifications are consistent with – and indeed more stringent than – the requirements of Article 29 of the Annex to the *Arrangement.* Brazil notes again that spare parts financing has been a *de minimis* element of PROEX III support in the past and that spare parts financing has been provided only in connection with sales of new aircraft.

Q12. With respect to Article 6 of Directive 374, what is the basis for Brazil's contention that this provision confers discretion on the Committee on Export Credits? (Brazil's first submission, para. 61) If the term "may" provides the basis for Brazil's contention, please also address the meaning of the term "may" in Article 2 of Directive 374.

Article 6 permits applicants to include spare parts financing in their application for equalization support and grants the Committee discretion to approve equalization for spare parts

(c) What are the benchmark "financing terms"? (Those available to the borrower in question? The industry sector in question?)

The financing terms in question refer to the terms that would be available for a comparable transaction for that buyer in the commercial marketplace. Please refer to the answer to question 2 above for further details.

(d) Do the financing "practices" referred to include officially supported financing?

As explained previously, there is no accepted definition of "officially supported financing." Article 88 of the *OECD Arrangement*, for example, states that it was not possible for the Participants to agree on a definition of the term. Moreover, as indicated in Article 86 of the *Arrangement*, there is considerable debate as to whether so-called "market window operations" – where government export credit agencies purport to be purely commercial actors in the market – are properly considered as "officially supported financing."

Furthermore, there are many different types of officially supported financing, and it will not always be clear what, if any, official support is included in a transaction in the market place. To the extent that a transaction appears to conform with the marketplace, then that transaction would be deemed to be part of the "practices" that would be examined by the Committee.

(e) What is the meaning of the phrase "shall have as reference"? Does this language enable the Committee to approve financing of operations on terms more favourable than those prevailing in the international market at the relevant time?

This phrase means the Committee must conform to the financing terms of the international market. The language prevents the Committee from approving financing on terms more favorable than those prevailing in the international market. Brazil notes, however, that there may be situations in which the CIRR is *below* the marketplace rates (Canada has previously explained that due to time lags in calculating the CIRR, the CIRR may be above or below the market at a given point in time)[9] In those circumstances, the Committee could provide PROEX support according to the interest rates provisions of the OECD Arrangement, and nevertheless benefit from the save haven of the second paragraph of item (k).

(f) Specifically, how would the Committee determine the net interest rate for eligible operations involving the export of regional aircraft in situations where the financing terms practised in the international market "justified" repayment terms of, e.g., 15 years?

The Committee would have to consider any proposal for financing that deviated from the CIRR based on the evidence placed before the Committee on a case-by-case basis. Brazil cannot comment on what that evidence may be for a future transaction. Brazil would note, however, that the CIRR may nevertheless be an appropriate rate for such a transaction, given that Canada has previously told the Panel that the terms in the marketplace may include interest rates below the CIRR (for Canada's "market window" financing) and loans with 15-18 year terms[10] In this instance, of course, the transaction would not be eligible for the safe haven of the second paragraph.

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[9] Brazil -- Export Financing Programme for Aircraft -- Recourse by Canada to Article 21.5 of the DSU, WT/DS46/RW para. 6.99 (9 May 2000).

[10] Article 21.5 Panel Report, page 81 (Canada's response to Question 2 posed by the Panel) and page 94 (Canada's response to Question 8 posed by Brazil).

(g) What is the relationship between Article 8, paragraph 2, and Article 1, paragraph 1? What of a case where reference to the financing terms practised in the international market would indicate an above-CIRR rate? Could the Committee still approve net interest rates at CIRR level?

The CIRR is intended to be the floor, or minimum possible net rate that may be approved by the Committee. As explained above, where the market is above the CIRR, the Committee nevertheless may approve financing at a net interest rate equal to the CIRR and still qualify for the safe haven of the second paragraph of item (k).

(h) What is the relationship between Article 8, paragraph 2, and Directive 374? In particular, which would take precedence if the financing terms practised in the international market "justified" (i) repayment terms in excess of 10 years, (ii) loan-to-asset values in excess of 85 per cent?

Article 8, paragraph 2 grants the Committee discretion to approve PROEX support so long as that support is consistent with the international market. Thus, the Committee would enjoy discretion under that paragraph to deviate from the terms of Directive 374. However, as discussed above, this discretion is not unlimited.

(i) With reference to para. 17 of Brazil's oral statement, please explain in what way Article 8, paragraph 2, of BCB Resolution 2799 adds to what is already stated in Article 1 thereof. In addition, does the reference to Article 8, paragraph 2, add anything to Article 2 of Provisional Measure 1629?

Article 1 of Resolution 2799 establishes the general framework for equalization payments under the PROEX programme. Article 8, paragraph 2, imposes a specific affirmative requirement on the Committee to ensure that any PROEX support, in addition to meeting the specific criteria enumerated elsewhere, is consistent with the terms practised in the international markets. Thus, Article 8 paragraph 2, uses the mandatory verb "shall" in describing the Committee's obligations.

Article 2 of Provisional Measure 1629 deals with types of financing not covered by Article 1 of the same Provisional Measure. Article 1 refers to post-shipment PROEX operations. These are the only types of operations for which regulations have been issued and that PROEX currently supports. They could involve both direct financing and equalization payments. Resolution 2799 implements Provisional Measure 1629 with regard to equalization payments only. Article 8.2 of Resolution 2799 ensures that the financing terms practiced in the international market will be used as the reference by the Comitê de Crédito às Exportações, when approving equalization payments concerning post-shipment financing transactions that do not conform to the general rules of the programme.

Article 2 of Provisional Measure 1629 contemplated equalization payments for pre-shipment financing. This mechanism has never been implemented and PROEX has never made equalization payments under this mechanism.

(Addressed to Both Parties)

Q21. On the assumption that the second paragraph of item (k) provides for an *exception* to the first paragraph thereof, would a Member invoking the second paragraph need to establish (i) that its internal law *allows* it to act in conformity with the interest rates provisions of the relevant OECD Arrangement or (ii) that its internal law *requires* it to act in conformity with the aforementioned interest rates provisions? If (ii) is correct, how does this view fit with the traditional distinction between mandatory and discretionary legislation in the GATT/WTO?

As a preliminary matter, Brazil wants to emphasize that it disagrees with the assumption that the second paragraph of item (k) provides for an exception only to the first paragraph of item (k). Under the second paragraph of item (k) "an export credit practice" which is in conformity with the interest rates provisions of the *OECD Arrangement* "shall not be considered an export subsidy prohibited by" the SCA Agreement. If the second paragraph of item (k) provided for an exception from the first paragraph only, "an export credit practice" must be understood to cover only practices within the scope of the first paragraph. In other words, "an export credit practice" must either be a "grant by governments" or a "payment" within the meaning of the first paragraph of item (k). Nothing in the plain meaning of the text can be interpreted to mean or even suggest that "an export credit practice" under the second paragraph of item (k) (or, indeed, under the *OECD Arrangement*) should be construed so narrowly. An export credit practice is a concept that is much broader than the scope of the first paragraph of item (k). The assumption that the second paragraph of item (k) provides for an exception only to the first paragraph would require Members to show that their export practices are a "grant" or a "payment" as defined by the first paragraph of item (k) before they can claim the safe haven.

The safe haven is thus an exception from Article 3 of the SCM Agreement. A subsidy contingent on exports that would otherwise be a prohibited subsidy would not be in breach of the SCM Agreement if it qualifies for the safe haven of the second paragraph of item (k) regardless of of th,e safe
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> 3.33 . . . the distinction in GATT 1947/WTO jurisprudence between discretionary and mandatory legislation is not based upon a particular provision of the WTO Agreement, nor is it limited in its application to a particular WTO provision . . .The distinction is a general principle developed by panels that most likely has its origin in the presumption against conflicts between national and international laws. It is both general international practice and that of the United States that statutory language is to be interpreted so as to avoid conflicts with international obligations. There is thus a presumption against a conflict between international and national law. In general [according to OPPENHEIM'S INTERNATIONAL LAW (hereinafter "OPPENHEIM'S")],
>
> > "[a]lthough national courts must apply national laws even if they conflict with international law, there is a presumption against the existence of such a conflict. As international law is based upon the common consent of the different states, it is improbable that a state would intentionally enact a rule conflicting with international law. A rule of national law which ostensibly seems to conflict with international law must, therefore, if possible always be so interpreted as to avoid such conflict."[12]

Both GATT and WTO Panels have relied on similar reasoning in applying the doctrine. Thus, in *Canada - Aircraft*, the Panel reviewed Brazil's allegation that two of the challenged programmes (Export Development Corporation and Canada Account) required Canada to grant subsidies. The Panel determined, however, that Brazil had not offered evidence demonstrating that subsidization was required under these programmes. Rather, "the grant of subsidies would be the result of the exercise of the administering authority's discretion in interpreting its mandate.[13] In these circumstances, the traditional distinction between discretionary and mandatory legislation prevented the Panel from making findings on the programmes *per se*, and instead required that Brazil establish

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Q22. The Panel in *United States – Section 301* (WT/DS152/R, para. 7.96) found legislation presumptively inconsistent with the *WTO Agreement* in a case where legislation provided discretion to act in a WTO-inconsistent manner. Do the findings of this Panel on this issue have any relevance to this dispute? Please elaborate.

Again, as Brazil noted above and during the meeting of the Panel, PROEX III does not allow Brazil to act in a manner that would be inconsistent with Brazil's WTO obligations. It requires that the authorities act in conformity with the provisions of the SCM Agreement. Therefore, the discretionary v. mandatory distinction and the findings in the *Section 301* case are irrelevant. However, even under the assumption that PROEX III is discretionary and allows Brazil to act in a manner inconsistent with the SCM Agreement, the findings of the *Section 301* Panel are not applicable because they are based on very different facts.

In *Section 301*The Panel in

there is no commercial reason why the level of spare parts financing in a given transaction would affect the interest rate for the transaction.

For these reasons, Brazil submits that the ordinary meaning of the term "interest rates provisions" in the second paragraph of item (k) is that it refers only to the provisions of the *Arrangement* that specify the interest rates. If the negotiators had meant to include other terms and conditions, they would have said so.

Brazil also notes that the second paragraph of item (k) purposefully refers to the "interest rates provisions" of the *Arrangement* rather than simply to the "provisions" of the *Arrangement*. In order to give meaning and effect to the inclusion of the words "interest rates" before the word "provisions,d

Published reports confirm that Air Wisconsin has bought Canadian, rather than Brazilian, regional jets.

Q2. Canada has provided evidence that Embraer recently offered PROEX financing to SA Airlink for a 15 year term. On 14 December 2000 Embraer announced the sale of up to 70 regional jets to SA Airlink. Has Brazil issued any letter(s) of commitment in respect of the SA Airlink sale *other than under PROEX III*? If so, will Brazil provide it/them to the Panel? Have any applications been made to the Committee on Export Credits or to any other authority of the Government of Brazil to provide financing in support of the SA Airlink sale? If so, will Brazil provide it/them to the Panel?

As Canada itself has acknowledged, the sole issue before this Panel is whether PROEX III constitutes a prohibited export subsidy. TD24Tw (caportthe GX) Tjm1rovide fdgedno0gc 1.15fore this ute

ANNEX B-6

**BRAZIL'S COMMENTS ON RESPONSES
TO QUESTIONS BY CANADA AND THIRD PARTIES**

(20 April 2001)

Canada's Replies

Question 15

1. Brazil finds Canada's response difficult to understand. Canada seems to be saying that PROEX can *never* be in conformity with the SCM Agreement because, "however it is delivered, it enables Brazil to continue to grant prohibited export subsidies." This contradicts prior statements of Canada. In its second oral statement to the original Panel, Canada stated that it "would not have brought this case" if only "PROEX simply reduced the net interest rate offered to an airline to one that is above LIBOR or OECD rates."[1] In responding to the questions of the first Article 21.5 Panel, Canada unambiguously stated that "the relevant benchmark against which a net interest rate must be compared to determine whether a material advantage has been secured is CIRR."[2] Canada's response appears to be just one more example of Canada's practice, indulged in throughout these proceedings, of constantly moving the goal post.

2. Canada also states that it "is also challenging PROEX III payments made in support of regional aircraft exports." Yet, Canada has been unable to point to a single instance of a PROEX III payment made in support of regional aircraft exports, for the very good reason that there have been none.

3. Canada's moving of the goal posts, and its reliance on non-existent transactions cannot obscure the fact that the sole issue before this Panel is not what PROEX I and II, provided, or how they were applied in practice. The sole issue is whether PROEX III, on its face, by its terms, conforms to Brazil's obligations under the SCM Agreement.

Question 16

4. Brazil believes that Canada has misinterpreted both Article 13 of the *OECD Arrangement* and the provisions of PROEX. While Brazil is not a Participant in the *Arrangement* and therefore was not privy to the intent of the Participants in its drafting, Article 13 does not appears to contain any mandatory provisions. Unlike, for example, Article 15 governing minimum interest rates (the parties "shall apply"), Article 13 merely states that parties shall "normally" require the repayment of principal to begin within six months. Further, Article 13(c) describes this as a "practice" rather than a "rulrat (and y* -00s a lo

12. In the second bullet point to its second paragraph, Canada seems to suggest that PROEX III does not qualify as "interest rate support" because it is a one-way flow from the government to the bank instead of a two-way flow, "associated with interest rate equalization." Canada neglects two important points. First, whatever the flow between the government and the bank is, the effect on the borrower is the same: the borrower always receives funds at the same rate. Second, in the case of a "two-way flow" the bank is always guaranteed its margin of profit. If it makes more than the agreed margin, it will have to pay the difference to the government, but if it makes less the government will compensate it for the difference. In the case of a "one-way" flow, the bank takes all of the risk: its profit margin is not guaranteed and it can still incur losses depending on how the market moves.

13. In the third bullet-point to paragraph 1 of its response, Canada appears to criticize Brazil for not providing enough support through PROEX. It may well be, as Canada says, that "Participants provide credit risk insurance or guarantees in conjunction with interest rate support to cover [the risk of non-repayment from the borrower]." If so, this is support that PROEX does not provide. PROEX provides no protection to the lender for possible default by the borrower.

14. Finally, Canada's assertion that "PROEX is divorced from the interest rate that prevails in the

18. Brazil must confess to some confusion about just what Canada's position is regarding the CIRR and the market. In paragraph six of its response to Question 18, Canada states that the airline with the best credit rating is American Airlines, and that the CIRR is 35 basis points lower than the rate American Airlines is able to achieve in the market. Canada made this point as well at paragraph 78 of its First Submission. As authority for the statement in its First Submission, Canada refers to page 13 of its Exhibit 17 which ostensibly shows that the debt of American Airlines trades at between 135 and 200 basis points above US Treasury rates which is, at a minimum, 35 basis points above the CIRR.

19. First, Brazil would point out that the securitization of aircraft *leases* is an operation that does not directly reflect the terms of the *original loan* itself. This complex and recently developed financial operation involves a number of additional steps. The enhanced equipment trust certificate ("EETC") securitization enhances the creditworthiness of traditional equipment trust certificates ("ETCs") secured by lease receivables and the leased aircraft as follows: first, the issuer of the EETCs is bankruptcy remote (and insulated from a bankruptcy of the lessee) to the satisfaction of the rating agencies; second, the EETCs are tranched to take advantage of the expected residual value of the aircraft, *i.e.*, the lower the advance level, the higher the rating; third, a liquidity facility is provided to ensure the continued payment of interest on the EETCs during the remarketing period following a possible default by the lessee. The term of the liquidity facility in an EETC securitization relies on the ability of a lessor to repossess an aircraft from a bankrupt lessee, if the lessee does not elect to perform.

20. The first EETC structure was closed by Northwest Airlines in 1994. As described above, the rating agencies concluded that the underlying corporate credit of a single airline could be enhanced through a combination of the ability to repossess and remarket the leased aircraft within a limited eighteen month period during which interest would continue to be paid by a liquidity facility. This was combined with tranched debt, to achieve ratings for all of the EETC classes of debt that were higher than that of the airline.

21. The securities of the EETC structure are offered in the secondary market and their prices then oscillate according to the financial market trends, with spreads that respond to various economic and market indicators (such as the behavior of the markets of stocks and bonds) that maintain no relationship whatsoever with the original financial structure of the loan obtained by the lessor when purchasing the aircraft. The spreads mentioned by Canada reflect nothing more than investors return expectations based on a range of commercial papers, with comparable coupons, yields, maturities, credit ratings, etc.

22. Canada's Exhibit 17 itself demonstrates the flaws in Canada's reasoning. With regard to its American Airlines illustration, on page 6 of Exhibit 17, it is stated that American Airlines "was placed on Watchlist negative by Moody's and CreditWatch negative by S&P after it proposed to acquire the assets of TWA and a portion of the assets of US Airways." This demonstrates that the papers from American Airlines today do not enjoy the same credit ratings that the airline once enjoyed.

23. Moreover, Canada's reliance on the January 2001 spread for American Airlines – or any airlines – is misplaced. That spread simply represents the current yield on the instrument. It has nothing to do with the original spread, at the time the EETCs were issued. In the case of American Airlines these ranged 112 to 147, considerably lower, but still above CIRR. However, as Exhibit 17 itself shows, many of the original spreads were below CIRR. This is the case for the very first transaction listed, for American [illegible] 75 Tc 0 TmanWairline a0p th6coupons, yields, maturities,

Exhibit 17. The offering spread on those transactions ranged from 90 to 100 – in other words, from 10 basis points below the CIRR to the CIRR. This transaction, as Exhibit 17 shows, was comparable to other rates at the time. It was also before PROEX III. More important, following Canada's logic with its American Airlines example, Embraer'rs paper today is trading at 115 to 160 points above the CIRR – so what is Canada's problem?

25. These distinctions between the securitization of leases and the terms of the original loan may be the key to understand Canada's departure from its previous statements defending the adequacy of the CIRR as a benchmark. As the panel recalls, before the *Canada – Aircraft* Panel, Canada said that the CIRR is, "by definition, 'close to commercial rates.'"[7] Moreover, before the Article 21.5 Panel in *Brazil – Aircraft*, Canada said that financing offered by its Export Development Corporation ("EDC") at rates *below* the CIRR were, nevertheless "commercial" and did not confer a benefit within the meaning of Article 1 of the SCM Agreement.[8]

26.

original Article 21.5 proceeding found difficult to meet, as does Canada here, albeit for different reasons.

31. The burden was impossible for Brazil because, while it was established that Canada provided support below the CIRR, Brazil could not establish with the required precision how far below Canada's rate was, and how that rate related to the market overall. Lack of transparency on the part of Canada and others in the market was a barrier Brazil could not surmount. Here, the barrier Canada cannot surmount is based on its unwillingness to disclose to the Panel the details of its own market operations. The consequence is, as Brazil noted above in its comment on Canada's response to Question 19, that Canada has offered only evidence of the secondary market for debt on large civil aircraft produced by Boeing, not for the original market for regional aircraft produced by Bombardier in which Canada participates.

Question 21

32. Canada's response admits that under the traditional distinction between mandatory and discretionary measures it is not sufficient to show that a measure might allow a Member to violate its WTO obligations but rather that the measure requires a Member to violate its WTO obligations. But then Canada argues that this distinction applies to every WTO provision with one exception: the second paragraph of item (k). Canada states that the mandatory v. discretionary distinction does not apply here because Brazil has the burden to establish an affirmative defense.

33. The premise of Canada's argument is false for several reasons. To begin with, Brazil's first

37. In this answer, Canada again refers to "evidence" that "establishes" Brazil's failure to comply with the interest rates provisions of the *Arrangement.* One assertion – that Directive 374 on its face allows financing for a period exceeding 10 years – will be addressed in Brazil's comments on Canada's response to Question 32. Brazil would like to point out, however, that Canada keeps referring to "unrebutted evidence" about Brazil's non-compliance without identifying that evidence. Brazil has submitted the evidence that must prevail in these proceedings: the documents constituting PROEX III. All Canada has submitted in exchange is newspaper reports. Canada has now – for the first time – attempted in its answers to claim that Directive 374 on its face allows financing for a period exceeding 10 years. As Brazil will show in its comment on Question 32, this assertion is untenable.

Question 22

38. Canada repeats its unsubstantiated assertion that Brazil has not shown that PROEX III allows for an application that is consistent with the SCM Agreement. Canada, however, has not, by any reasonable standard, even remotely made a *prima facie* case that PROEX III *requires* a violation of Brazil's WTO obligations.

39. Further, Canada misinterprets the *Section 301* case. It is incorrect to state, as Canada does, that "the *Section 301* panel found legislation to be presumptively inconsistent with the WTO Agreement in a case where legislation provided discretion to act in a WTO-inconsistent manner." In *Section 301*, the US legislation *required* USTR, under certain circumstances, to make a unilateral determination on whether another government acted in compliance with its WTO obligations. While USTR retained the discretion to determine whether another government acted in compliance with its WTO obligations, it was required by the legislation to make that determination unilaterally. Thus, the *Section 301* finding is not inconsistent with the traditional mandatory v. discretionary distinction and is not applicable to the facts of this case. PROEX III, contrary to Canada's assertion, does not *require* that Brazil act in a manner inconsistent with its WTO obligations.

Question 23

40. Brazil has not granted any subsidies under PROEX III; therefore, Brazil does not maintain any subsidies under PROEX III.

Question 24

41. B 69nad9"om TDTnlale

Question 25

44. Brazil already has enumerated the provisions of the OECD Arrangement it considers as "interest rates provisions" and will not now restate those provisions. However, Brazil disagrees with Canada's views on this issue and has the following comments.

45. Canada states that its interpretation encompasses provisions that "affect what the interest rate and the amount of interest payable will be in a given transaction." However, many of the provisions

what the drafters said or intended to day. In fact, such an interpretation would probably have never occurred to them had Canada not advanced it in these proceedings.

50. The Portuguese phrase "poderá ser ampliado para até" means "may be extended up to" ("jusqu'à" in French, "hasta" in Spanish). The Annex to Directive 374 provides for the maximum term of financing for the specific categories of goods, category by category. For aircraft, it is a maximum of 10 years. Article 3, paragraph 2 of Directive 374 provides that the term of interest rate support may be extended up to a certain period contingent upon the value of the goods.

51. Thus, for example, according to the Annex, the term for interest rate support for balloons cannot exceed 7 months. Under Article 3, paragraph 2, assuming balloons are in the first category, between $1,000 and $5,000, the maximum tenure can be extended from 7 months up to a maximum of 12 months. The provision of Article 3, paragraph 2, is not relevant for aircraft. The maximum term under that provision is 8 years. The provision of the Annex, specific to aircraft, allows financing for a maximum term of up to 10 years. Thus, the ceiling under the Annex is higher than the ceiling of Article 3, paragraph 2, and no further extension is allowed. As Brazil has stated on numerous occasions, the exception from this rule can be based only on the provision of Article 8, paragraph 2 of Resolution 2799 which allows the Committee to extend the term of financing if different terms are available in the international market.

Third Party Responses

European Communities' Responses

Question 27

52. Brazil agrees with the EC's statement in its response to Question 26 that PROEX III "is therefore interest rate support within the meaning of Article 2." However, Brazil does not agree with several points raised by the EC in its response to Question 27.

53. The EC at great length discusses risk premiums, but the 1998 version of the *Arrangement* refers only to country risk, not to company risk, and, as the EC admits, those country risk benchmarks are not available to non-participants. There are no references to risk premiums in the 1992 version of the *Arrangement*, the version that was incorporated by the WTO in 1995.

54. In Brazil's view, the point made by the EC in paragraph 7 of its response demonstrates forcefully why the term "interest rates provisions" in the *Arrangement* should be interpreted narrowly, and why the Panel should conclude that it is the 1992 version of the *Arrangement* that is relevant, not the 1998 version, adopted three years after the WTO came into being.

55. The EC describes the OECD and its *Arrangement* as if it were an exclusive club, which perhaps it is. The *Arrangement* is a "gentlemen's agreement" and, "One consequence of this is that circumvention of its provisions is not considered legitimate." However, WTO Members are entitled to know with reasonable clarity and precision what rules they are and are not expected to observe. They are not to be left to the vague standards of etiquette that a group of gentlemen sitting in Paris consider appropriate.

Korea's Response

Question 26

56. Note 53 from the original Article 21.5 Panel Report, quoted by Korea in its response, is a generally accurate description of PROEX III.

Question 27

57. Korea accurately observes that, "The concept of minimum premiums does not apply to interest rate support" and that the *Arrangement's* minimum premium benchmarks are not even available to non-Participants.

United States' Response

Question 26

58. Brazil agrees with the statement of the United States, in the first paragraph of its answer, that, "The purpose of the [OECD] arrangement is to allow the commercial bank to provide fixed rate financing at the appropriate CIRR rate." This is precisely what PROEX III does.

59. The United States goes on, in that paragraph, to describe much of what PROEX III does *not* do. PROEX does *not* compensate the bank for its own floating rate funding risk. Beyond its fixed, maximum 2.5 percent payment, PROEX does *not* pay interest rate shortfalls to the bank depending upon the relationship between the fixed rate of the loan and the floating rate during the life of the loan. If, as the United States maintains, "most OECD governments offering interest rate support" also offer this kind of protection, they are offering much more than PROEX III offers.

60. PROEX III meets the criteria the United States sets out in the second paragraph of its response: (a) the interest rate the borrower sees after the interest rate support is the appropriate CIRR and (b) PROEX is not offered in a manner or at a level that is used to cover other costs of the borrower.

Question 27

61. The US states that "when a government does offer interest rate support in conjunction with insurance or a guarantee, the government must charge the appropriate minimum premium rate because it is providing insurance or guarantee cover." Thus, the US acknowledges that the only reason to charge a premium rate is to cover insurance or a guarantee – not for interest rate support. Since PROEX III does not provide insurance or guarantee cover, there is no need for a premium.

62. In the second paragraph of its answer (paragraph 4 of the document) the United States provides the web address of the OECD for the benefit of Brazil and the other 110 or more non-participant WTO Members. The EC, in its Third Party Submission – *noblesse oblige* – was good enough to do the same. While it is kind of the US and the EC to tell Brazil and the rest of the developing world how to find the OECD on the web, the point is that WTO Members should not be required to check the web site of the OECD in order to learn the nature of their WTO obligations. This is all the more reason why the Panel should conclude that the 1992 version is the relevant version of the *Arrangement* for purposes of item (k) second paragraph.

Question 29

63. The US admits that *Arrangement* Participants make notifications of non-conforming terms available to each other, but not to non-participants. While the US states its willingness to support reform of this procedure within the OECD, this is hardly a compelling argument for concluding that non-participants should be bound by the provisions concerned. It also demonstrates the elusive and changing character of the "gentlemen's agreement," and is further argument why the more clear, and now fixed, terms of the 1992 version of the *Arrangement* are those that were incorporated into item (k) second paragraph.