THIRD PARTY SUBMISSION OF NEW ZEALAND

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I. INTRODUCTION

1.01 The rulings and recommendations of the panel and of the Appellate Body in *United States – Subsidies on Upland Cotton* adopted by the Dispute Settlement Body ("DSB") on 21 March 2005 constituted an important step in the interpretation and application of the provisions of the *Agreement on Subsidies and Countervailing Measures* ("SCM Agreement") in respect of both prohibited and actionable subsidies. In particular it clarified the meaning and scope of the concept of serious prejudice in Article 6 of the SCM Agreement. New Zealand was a third party in that case because of its systemic interest in the integrity of these provisions. As a leading agricultural exporter New Zealand has a particular interest in the application of the subsidies disciplines to agricultural products. Thus, New Zealand welcomed the adoption of the panel and Appellate Body reports.

1.02 Brazil now brings the matter of United States subsidies in respect of upland cotton back under Article 21.5 of the Dispute Settlement Understanding (DSU). Brazil argues that the United States action and inaction in respect of the recommendations and rulings of the DSB puts it in violation of its obligations under Articles 5 and 7.8 of the SCM Agreement. Failure by the United States to remove the adverse effects or withdraw the subsidising measures as required by Article 7.8 of the SCM Agreement, calls into question the very viability of the disciplines in that Agreement. As a result, New Zealand is exercising its right as a third party in this Article 21.5 compliance proceeding.

1.03 In New Zealand's view, the decision of the panel in this case will have far-reaching implications. Not only is the fact of non-compliance a threat to the subsidy disciplines of the SCM Agreement, but the arguments put forward by the United States in its response to the claim of Brazil have serious systemic implications for the future application of the SCM Agreement. New Zealand will elaborate on this aspect throughout this submission.

II. THE FINDINGS IN QUESTION AND THE ALLEGED MEASURES OF IMPLEMENTATION

2.01 In this submission New Zealand will focus on the implementation of the recommendations and rulings of the DSB in respect of the subsidies that were found by the panel in the original proceedings to be actionable. The relevant part of the panel's findings is paragraph 8.1(g)(i) which provides:

> the effect of the mandatory price-contingent United States subsidy measures – marketing loan programme payments, user marketing (Step 2) payments, MLA payments and CCP payments - is significant price suppression in the same world market within the meaning of Article 6.3(c) of the *SCM Agreement* constituting serious prejudice to the interests of Brazil within the meaning of Article 5(c) of the *SCM Agreement*;

2.02 In paragraph 8.3 the panel went on to say in respect of its finding in paragraph 8.1(g)(i), that in light of Article 7.8 of the SCM Agreement the United States was under an obligation to "take appropriate steps to remove the adverse effects … or withdraw the subsidy". The Appellate Body expressly upheld the finding of the panel in paragraph 8.1(g)(i).

2.03 As Brazil has pointed out, the only action taken by the United States in implementing the recommendations and rulings of the DSB on 21 March 2005 has been the abolition of user marketing (Step 2) payments. The programmes under the Farm Security and Rural Investment ("FSRI") Act of 2002 providing for marketing loan payments and counter-cyclical payments remain. Since these were the major contributors to the price suppression and hence the serious prejudice found by the panel then, as Brazil argues, the United States has failed to remove the adverse effects as required by Article 7.8 of the SCM Agreement and thus remains in violation of Article 5 of the SCM Agreement.

2.04 The United States response falls into two broad areas. First, the United States argues that certain claims made by Brazil are outside the scope of DSU Article 21.5 proceedings and requests that the panel make preliminary rulings to that effect. Second the United States claims that Brazil has failed to show that in the absence of the Step 2 payments, the marketing loan and counter-cyclical programmes cause serious prejudice either through price suppression or through an increase in world market share. In New Zealand's view both of these arguments are flawed. In this submission, New Zealand will provide some comments on the United States claims. In respect of the request for preliminary rulings, New Zealand will focus on the claim that the marketing loan and counter-cyclical programs are outside the scope of these Article 21.5 proceedings.

III. DSU ARTICLE 21.5 AND SCM AGREEMENT ARTICLE 7.8

3.01 Before addressing the United States preliminary rulings claim, New Zealand wishes to make some comments on the uniqueness of this case and the importance of its implications. This Article 21.5 proceeding involves for the first time the question of compliance in respect of the obligation under Article 7.8 of the SCM Agreement either to withdraw the subsidy or to "take appropriate steps to remove the adverse effects". Hence this panel is faced with the interpretation of both DSU Article 21.5 and Article 7.8 of the SCM Agreement and with determining their relationship to each other.

3.02 DSU Article 21.5 mandates a panel to consider "the existence or consistency of measures taken to comply with the recommendations and rulings" of the DSB. As the Appellate Body has pointed out, this provision entitles a panel to determine whether any measures exist to implement the recommendations and rulings of the DSB.[1] However, when compliance with Article 7.8 of the SCM Agreement is raised in an Article 21.5 proceeding, it is not just a question of the existence of measures or of their consistency with the recommendations and rulings of the DSB that has to be considered. If the subsidising measures in question have not been withdrawn then there is the further question of whether "appropriate steps" have been taken to remove the adverse effects of those measures.

3.03 In New Zealand's view, an enquiry to determine whether Article 7.8 of the SCM Agreement has been complied with can involve a panel in looking at three things. First, a panel must determine whether the subsidising measures have been withdrawn. Second, if those measures have not been withdrawn, then the panel must consider whether any steps have been taken to remove the adverse effects. Third, if the panel finds that steps have been taken to remove the adverse effects, then it must determine whether those steps are "appropriate".

3.04 In New Zealand's view, the steps would only be "appropriate" if they are capable of removing the adverse effects. The *Oxford English Dictionary* defines "appropriate" as meaning "specially fitted, suitable, proper".[2] A measure that is not capable of achieving its objective of removing the adverse effects would be neither suitable nor appropriate. As a consequence, steps taken by an implementing Member that are not capable of removing the adverse effects would not be "appropriate steps" within the meaning of Article 7.8 of the SCM Agreement.

IV. THE PRELIMINARY RULINGS CLAIM

4.01 The United States claims that marketing loans and counter-cyclical programmes under the FSRI are "outside the scope" of the Article 21.5 proceeding. The United States presents two arguments in this respect. First, it argues that the DSB ruling covered only certain "payments" under those programmes, not the programmes themselves. Second, the United States argues that these

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[1] Appellate Body Report, *United States – Tax Treatment for "Foreign Sales Corporations" – Second Recourse to Article 21.5 of the DSU by the European Communities*, WT/DS108/AB/RW2, 14 March 2006, para. 93.

[2] *The Oxford English Dictionary* (2nd Edition) – Volume I, Clarendon Press, Oxford: 1989, p. 586.

programmes do not constitute "measures taken to comply" with the recommendations and rulings of the DSB and hence they fall outside the scope of DSU Article 21.5. In New Zealand's view both arguments are unsupportable. Moreover, if these arguments were to be upheld, the actionable subsidy regime under the SCM Agreement would be completely undermined.

4.02 New Zealand notes that the United States also requests a preliminary ruling that Brazil's claim that no action was taken by the United States in implementation of the recommendations and rulings of the DSB between 21 September 2005 and 31 July 2006 is also outside the scope of these proceedings. On this matter, however, Brazil is undoubtedly correct. The United States cannot claim that since it took no implementing action until 1 August 2006, that period is outside the scope of these proceedings. DSU Article 21.5 applies to the "existence" of measures not just to the consistency of measures actually taken to comply with the recommendations and rulings of the DSB.

A. THE PAYMENTS/PROGRAMMES DISTINCTION

4.03 The United States claim that the panel's finding in paragraph 8.1(g)(i) is limited to specific payments and did not cover the programmes that authorise those payments involves a rewriting of the panel's findings. The United States seeks to revise the finding of the panel in light of certain arguments made by Brazil in the panel proceedings, but there is no justification for rewriting the conclusions of the panel in this way.

4.04 An examination of the panel's finding indicates that the United States contention simply has no basis. In paragraph 8.1(g)(i) the panel made a finding about "the effect of the mandatory price-contingent United States subsidy measures". The finding was that these measures constituted "significant price suppression". The descriptive reference to "marketing loan programme payments, user marketing (Step 2) payments, MLA payments and CCP payments" does not alter the nature of the finding. Payments are not mandatory subsidy measures; they are simply the means by which the subsidy measures are implemented.

4.05 Moreover, it is quite clear that the panel's analysis of the subsidy measures that caused price suppression was of the programmes under the FSRI under which payments are made. The panel determined that the marketing loan payments are mandatory by reference to the "text of the measure".[3] The "measure" here is the marketing loan programme, not the payment itself. The panel states, "the structure, design and operation of the marketing loan programme has enhanced production and trade-distorting effects"[4]. Again, it is the programme under which the payments were made that was being considered by the panel, not just specific payments.

4.06 The United States claims that the statement of the panel in paragraph 7.1501 that "the United States is obliged to take action concerning its present statutory and regulatory framework as a result of our ‘present' serious prejudice finding" is not a recommendation of the panel, and thus presumably is not binding on the United States. What this argument ignores, however, is that although not a recommendation as such, the statement is relevant to understanding the findings of the panel. It gives meaning to the finding in paragraph 8.1(g)(i) relating to the "United States subsidy measures" that constituted significant price suppression.

4.07 In short, read properly in the context of the panel's decision as a whole, the finding in paragraph 8.1(g)(i) is not limited to the specific payments in MY 1999-2002. It applies to the measures under which those payments are authorised and hence to the marketing loan and counter-cyclical programmes themselves.

[3] Panel Report, *United States – Subsidies on Upland Cotton* WT/DS267/R, 8 September 2004, paragraph 7.1291.

[4] *Ibid*, paragraph 7.1295.

4.08 Moreover, the United States distinction between payments and programmes leads to an absurd result. It means that serious prejudice would have to be proved annually in the light of payments that have been made by which time the adverse effects have already occurred and it would be too late to withdraw the measure that caused them. To argue that the panel was referring only to payments in MY 2002 makes nonsense out the panel's own reference to Article 7.8 of the SCM Agreement and to the requirement to withdraw the subsidy. How can a subsidy be withdrawn if in fact the subsidy is over and the subsidizing effect is past? The United States arguments would simply undermine the disciplines on actionable subsidies in the SCM Agreement.

B. THE "MEASURES TAKEN TO COMPLY" ARGUMENT

4.09 The United States also argues that the marketing loan and counter-cyclical payments programmes are outside the scope of these Article 21.5 proceedings because they are not "measures taken to comply with the recommendations and rulings" of the DSB. According to the United States, "Article 21.5 applies only with respect to a disagreement as to the existence or consistency of a measure taken to comply", hence it cannot apply to programmes that existed at the time the matter came before the original panel and are unchanged. Under the United States logic, any such challenge to these measures has to be the subject of a new complaint.

4.10 In New Zealand's view, the United States argument ignores the fact that Article 21.5 is not the only relevant provision in these proceedings. In respect of the panel's finding under paragraph 8.1(g)(i), the obligation on the United States is found in Article 7.8 of the SCM Agreement. This provision grants the United States the choice either to withdraw the measures in question or to remove the adverse effects. Having chosen not to withdraw the marketing loan and counter-cyclical payments programmes, the United States cannot now avoid its obligation under Article 7.8 of the SCM Agreement to remove the adverse effects of those subsidy programmes by claiming that they are not measures taken to comply within the meaning of DSU Article 21.5. The United States cannot use the provisions of Article 21.5 to nullify its obligation under Article 7.8 of the SCM Agreement.

4.11 As pointed out in paragraphs 3.03 and 3.04 above, in applying Article 7.8 of the SCM Agreement to the present case the panel has to determine whether the measures causing serious prejudice have been withdrawn. In the case of the marketing loan and the counter-cyclical payments programmes they have not been withdrawn. The panel must then determine whether steps have been taken to remove the adverse effects found to exist by the original panel. It must then determine whether any steps that have been taken are "appropriate", that is whether they are measures that are capable of removing the adverse effects. DSU Article 21.5 cannot be invoked, as the United States seeks to do in this case, as a barrier to the panel conducting such an analysis.

V. THE SUBSTANTIVE CLAIMS

5.01 Brazil argues that even in the absence of the Step 2 payments programme, marketing loan payments and counter-cyclical payments alone cause significant price suppression. Indeed, Brazil argues that the removal of the Step 2 programme could increase counter-cyclical payments, thus adding to the significant price depression. Brazil also argues that marketing loan and counter-cyclical payments threaten to cause serious injury in MY 2006 and beyond. New Zealand supports these claims.

5.02 The United States response falls into three broad categories. First the United States argues that Brazil has not substantiated its claim that the effect of the Step 2 payments on price suppression was "relatively modest". Second the United States claims that Brazil is in effect arguing that the marketing loan and counter-cyclical payments *per se* violate the WTO Agreements, and that this could only occur if the programmes "mandate a breach" of those agreements, which the United States claims that they do not. Thirdly, the United States argues that Brazil has failed to make a *prima facie* case of the WTO inconsistency of the marketing loan and counter-cyclical payments programmes.

5.03 New Zealand will comment on each of these arguments, but before doing so will make a preliminary observation about the implications of the United States arguments in the context of an Article 21.5 case where the central question is whether there has been compliance with Article 7.8 of the SCM Agreement.

5.04 The essence of the arguments of the United States is that Brazil has the burden of showing that in the light of the removal of the Step 2 payments programme the marketing loan and counter-cyclical payments programmes cause or threaten serious prejudice, and it has failed to meet that burden. There is no doubt that as complainant in this Article 21.5 proceeding Brazil bears the burden of proof.[5] The question is what does such a burden entail?

5.05 In the present case, the DSB recommendations and rulings of 21 March 2005 covered three programmes; the Step 2 payments programme, the marketing loan payments programme and the counter-cyclical payments programme. But having chosen to remove only one of those programmes, the United States now claims that Brazil has the burden of showing that the remaining two programmes cause serious prejudice. Thus, in substance the United States is claiming that Brazil must prove again what it had already proved and what has been already been found by the original panel to cause serious prejudice. This cannot be the intent of either DSU Article 21.5 or Article 7.8 of the SCM Agreement. A Member should not have the burden of proving something that has already been decided by the original panel.

5.06 In New Zealand's view, Article 7.8 of the SCM Agreement operates to distribute the burden of proof somewhat differently. Since an implementing Member has the option of either withdrawing the subsidising measure or removing the adverse effects, a Member that fails to withdraw the measure in question then should have the burden of showing that it has removed the adverse effects. Thus, in the present case proof by Brazil that the measures found by the original panel to cause adverse effects have not been withdrawn should establish a *prima facie* case that implementation has not occurred and the burden should then shift to the United States to prove that the adverse effects caused by those subsidising measures have been removed.

A. THE UNITED STATES CLAIM THAT THE IMPACT OF THE REMOVAL OF STEP 2 PAYMENTS IS NOT "RELATIVELY MODEST"

5.07 Much of the United States argument that Brazil is incorrect in treating the impact of the removal of Step 2 payments as "relatively modest" is focused on what it perceived Brazil to be arguing before the original panel. But this is simply not relevant. Rather, it is what the panel decided and the actual impact of the removal of the Step 2 payment programme that is relevant. The original panel concluded that the marketing loan and counter-cyclical payments programmes contributed to price suppression and serious prejudice. In its First Written Submission Brazil has demonstrated that notwithstanding the withdrawal of the Step 2 payments programme, payments under the marketing loan and counter-cyclical payments programmes caused price suppression in the world market in MY 2005 and an increase in United States world market share in upland cotton in MY 2005. Thus, there is serious prejudice within the meaning of SCM Article 5(c).

5.08 The United States claim about the significance of the removal of the Step 2 payments programme is undermined by a comparison of the amounts paid under the various programmes. Step 2 payments are small compared to marketing loan and counter-cyclical payments. In the most recent year, 2005, for example, the Step 2 payments amounted to US$350 million. In the same year,

[5] Appellate Body Report, *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India*, WT/DS33/AB/R, 25 April 1997, p. 14.

the marketing loan and counter-cyclical programme payments amounted to US$2,170 million.[6] Similar ratios existed in most other years. There is no doubt that the removal of the Step 2 payment programme had some impact, but the United States cannot ignore the much larger volume of subsidisation under the two programmes that have not been withdrawn or modified.

5.09 The United States also seeks to counter Brazil's argument that eliminating Step 2 payments could result in a higher counter-cyclical payment rate by arguing that in the current year there could not be any increase in counter-cyclical payments. But, this is because counter-cyclical payments are already at their maximum rate.[7] In other words, the United States is not arguing that the counter-cyclical programme would not compensate for the elimination of the Step 2 payments; rather, it is arguing that payments are already so high that under current conditions no further payments can be made. None of this supports the United States contention that the programme does not have a price suppressing effect.

5.10 The United States also contends that Brazil fails to recognize that the elimination of Step 2 payments will result in a lowering of marketing loan payments. While this may be true because marketing loan payments are configured on world prices, which would increase with the elimination of Step 2 payments, what the argument ignores is the fact that these programmes are distorting whether or not payments are made under them. It is the programmes themselves not the payments that create expectations. Producers know that the loan rate is there to support them, that there is a target price[8] that they will receive either from the market or from the government. Neither the elimination of Step 2 payments nor any lowering of marketing loan payments in fact diminishes the distorting effect of the marketing loan and counter-cyclical programmes.

5.11 Finally, even the United States own figures show that the impact of the elimination of the Step 2 payment programme is modest. On one occasion it cites an increase of 0.4c/lb in the adjusted world price or $2.25 per ha[9] and on another occasion it cites an increase in the world price of 1.4c/1b or $2.30 per ha.[10] By comparison with the futures price in 2005-2006 (52.9-59.35 cents per pound)[11], loan rate (52 cents per pound)[12] or target price in the same period (72.4 cents per pound)[13], this effect on world prices of the elimination of the Step 2 payment programme is indeed "relatively modest".

5.12 The United States arguments leave intact the fundamental point made by Brazil, that even in the absence of the Step 2 payment programme, the marketing loan and counter-cyclical programmes still result in significant price suppression within the meaning of Article 6.3(c) of the SCM Agreement and thus cause serious prejudice contrary to Article 5(c) of the SCM Agreement.

B. THE UNITED STATES CLAIM THAT MARKETING LOAN AND COUNTER-CYCLICAL PAYMENTS PROGRAMMES DO NOT MANDATE A BREACH OF THE WTO AGREEMENTS

5.13 The United States claims that Brazil cannot challenge the marketing loan and counter-cyclical payments programmes unless it can show that these programmes mandate a breach of the WTO agreements. In the United States view, to do so Brazil would have to show that these programmes mandated actions that must lead to the effect of causing serious prejudice to Brazil, and Brazil has not done so.

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6 *United States – Subsidies on Upland Cotton – Recourse by Brazil to Article 21.5 of the DSU* (DS267), First Written Submission of Brazil, 17 November 2006, ("Brazil First Written Submission"), para. 111, and Table 6.

7 *United States – Subsidies on Upland Cotton – Recourse by Brazil to Article 21.5 of the DSU* (DS267), First Submission and Request for Preliminary Rulings of the United States, 15 December 2006, ("United States First Written Submission"), para. 162.

8 United States First Written Submission, para. 161.

9 United States First Written Submission, para. 174.

10 United States First Written Submission, para. 169.

11 United States First Written Submission, para. 231.

12 *Ibid*.

13 United States First Written Submission, para. 161.

5.14 Once again, the United States is ignoring the fact that the original panel had already determined that payments under the programmes in question caused serious prejudice to Brazil. Equally, the United States is ignoring the fact that the question in this case is not whether the programmes in question require that adverse effects are caused to Brazil, but whether the United States has taken appropriate steps to remove the adverse effects found by the original panel to exist as a result of the operation of these programmes. In this context, the mandatory/discretionary distinction called in aid by the United States is simply irrelevant.

C. THE UNITED STATES CLAIM THAT BRAZIL HAS FAILED TO MAKE A *PRIMA FACIE* CASE OF WTO INCONSISTENCY OF THE MARKETING LOAN AND COUNTER-CYCLICAL PAYMENTS PROGRAMMES

5.15 As pointed out earlier, the United States arguments on the WTO-consistency of the marketing loan and counter-cyclical payments programmes are tantamount to placing on Brazil a burden to prove once again what it had already proved before the original panel. In New Zealand's view such an approach to the application of Article 7.8 of the SCM Agreement risks depriving the actionable subsidies provisions of the SCM Agreement of their proper effect. Furthermore, New Zealand sees many of the arguments of the United States as attempts to reargue what it argued before the original panel, and lost. Again, such an approach is consistent with the objectives of neither DSU Article 21.5 nor Article 7.8 of the SCM Agreement.

1. Counter-cyclical Payments

5.16 The United States attempts to counter Brazil's arguments about the trade-distorting effects of counter-cyclical payments by blurring the line between counter-cyclical payments and decoupled payments. Thus, it cites studies relating to decoupled payments and says that they provide "valuable insights".[14] The United States also refers to studies concerning general wealth risks[15], as if they were equally applicable to the revenue risk that counter-cyclical payments are concerned with, again treating counter-cyclical payments as co-extensive with decoupled payments. But counter-cyclical payments are not real decoupled payments.

5.17 Real decoupled payments are green box measures and as defined in Annex 2 of the Agreement on Agriculture cannot be linked to the type or volume of production (paragraph 6(b)), or be related to or based on prices (paragraph 6(c)). Counter-cyclical payments, by contrast, are clearly and explicitly linked to prices. The fact that in many years such payments are likely to be paid out at the maximum rate[16] does not change the fact that they are linked to prices. The question is what would farmers do differently if there were no counter-cyclical payments and farmers were, essentially, "guaranteed" 13.73c/lb less for their cotton? Counter-cyclical payments are clearly not green box measures and hence are presumptively trade distorting.

5.18 The same fallacy of linking counter-cyclical payments to decoupled payments is found in the United States arguments about the increase in wealth from counter-cyclical payments accruing to non-operator landlords and hence capitalised into higher land values.[17] While this is certainly true of real decoupled payments, it is simply not plausible in the case of counter-cyclical payments. What producer is going agree to the "modified rental arrangements" that the United States refers to[18], when counter-cyclical payments could be at 13.73 c/lb one year and at zero the next?

[14] United States First Written Submission, para. 213.
[15] United States First Written Submission, para. 209.
[16] United States First Written Submission, para. 211.
[17] United States First Written Submission, paras. 216-219.
[18] United States First Written Submission, para. 216.

2. Marketing Loan Payments

5.19 The United States claims that Brazil has failed to demonstrate that marketing loan payments are having significant price-distorting effects. Yet the proposition that marketing loan payments are distorting is almost self-evident. Marketing loan payments are amber box measures, the category in which are included the non-prohibited measures with the most distorting effect on production and trade.

5.20 Moreover, the United States arguments about marketing loan payments ignore once again that it is the expectations of producers that are important and that those expectations are generated because of the existence of the applied administrative prices under the marketing loan programme, not because of the financial transfers in any year. Thus, the United States argument that since cotton futures prices in MY 2006 were higher than the loan rate then the loan rate would have no effect on producers planting decisions[19] misses the point. First, the loan rate will not always be below the futures prices; in some years there have been large amounts paid out under the marketing loan programme.[20] Second, the programme offers a guarantee by the government that producers will receive a particular price whether they are involved in the futures market or not.

5.21 Furthermore, the United States claims that at the time of planting producers "*did not expect*" that they would receive these payments on harvest[21] is a clever play on the word "expect". No doubt producers hoped that they would receive a higher price. But what they certainly expected was that they would receive at least the guaranteed price of 52c/lb, regardless of what happened in the market place, because that is what the law mandated. As the Appellate Body pointed out in the original proceeding[22]:

> … although farmers had expected higher prices in making their planting decisions, they were also aware that if actual prices were ultimately lower, they would be "insulated"[23] by government support, including not only marketing loan program payments but also counter-cyclical payments, …

5.22 Thus, it was the guarantee of insulation that was affecting planting decisions – whether the price was received from the market or the government was immaterial. In fact, it is most unlikely that the farmers give the same weight to futures prices as to the guaranteed loan rate. To do so would require them to sell all their crops forward at the future rate and take the risk that their actual production would allow them to meet their forward commitments – in effect to take the production risk from which marketing loan programme payments based on actual production was protecting them.

3. Marketing Loan and Counter-Cyclical Payment Programmes and Market Signals

5.23 Much of the United States argument is directed to trying to demonstrate a link between producer decisions and market signals. However, the United States does not and cannot demonstrate that planting decisions of producers were shaped by market factors. The United States failed to do so before the original panel and the Appellate Body, and its attempt to reargue the matter in these Article 21.5 proceedings is equally ineffective.

5.24 The United States argues that the fact that the United States share of production has been stable over the life of the marketing loan and counter-cyclical programmes indicates that the

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[19] United States First Written Submission, para. 230.

[20] United States First Written Submission, para. 248.

[21] United States First Written Submission, para. 231. (Emphasis in original.)

[22] Appellate Body Report, *United States – Subsidies on Upland Cotton*, 3 March 2005, WT/DS267/AB/R, ("*U.S. – Upland Cotton (AB)*"), para. 445.

[23] Panel Report, *United States – Subsidies on Upland Cotton*, 8 September 2004, WT/DS267/R, ("*U.S. – Upland Cotton (Panel)*"), para. 7.1294.

programmes are not insulating producers from market signals.[24] But, the question is not whether United States share of production has been stable it is whether in the absence of the marketing loan and counter-cyclical payments programmes the United States market share would be at current levels. And the answer to that question would have to be no. The United States says that Brazil's claim that "*But for* the effect of price-contingent U.S. marketing loan and counter-cyclical payments, it would be expected that non-subsidized producers, such as those in Brazil and West and Central African countries, would have significantly increased their share of production and exports in the world market"[25] simply assumes its own conclusion.[26] But this is just assertion not argument, and thus the United States has no response to Brazil's position.

5.25 The United States argues that there is an inconsistency between Brazil's assertion that there is no link between prices and United States acreage, production and exports, and its claim that the United States is the single most important market influencing world market prices.[27] If the United States is the single most important market influencing world prices, the United States says, then surely there must be a link between world prices and United States planted acreage, production and exports. But the inconsistency is of the United States own making. The link is not between world prices and United States production. It is between domestic, guaranteed prices and United States production. And, that of course, is the source of the problem.

5.26 The United States claim that at the time of planting a farmer "cannot *know* what final prices and final costs will be,"[28] says less than meets the eye. What the farmer does know is that for all cotton harvested the price will be at least the loan rate. In addition, if market price is not significantly above the loan rate and the planting is on base acres there will be a counter-cyclical payment top-up (albeit based not on actual production, but on average yields in earlier years). So, if the farmer continues to produce cotton the expected return is going to be around the target price for most production on base acres. By contrast, cotton producers in Africa or Brazil know that they will get only the world price – whatever that is.

5.27 The United States contests Brazil's claim that the marketing loan and counter-cyclical payments programmes play an essential role in ensuring that producers cover their long-term costs of production and that in the absence of these programmes producers would switch to alternative crops.[29] It is, in the United States view, variable costs not long-term costs that influence the decision on whether to continue or exit cotton farming. However, the United States claim that Brazil has provided no evidence that absent the payments farmers would exit cotton production[30] ignores the evidence that Brazil provides in fact.

5.28 In paragraph 11 of its First Written Submission, Brazil provides a table indicating total United States subsidies for upland cotton from MY 1999 to the present which demonstrates that in some years over half of the revenue received by United States cotton farmers comes from subsidies. The idea that if these subsidies were not there, producers who have been deprived of half of their income would carry on planting cotton – business as usual – is little short of absurd. Brazil also points out that without marketing loan and counter-cyclical payments between MY 2000-2005 United States cotton producers would have lost US$663 per acre.[31] No rational economic operator would continue to plant cotton under such conditions.

[24] United States First Written Submission, para. 243.
[25] Brazil First Written Submission, para. 90.
[26] United States First Written Submission, para. 251.
[27] United States First Written Submission, para. 254.
[28] United States First Written Submission, para. 255. (Emphasis in original.)
[29] United States First Written Submission, para. 292.
[30] United States First Written Submission, para. 297.
[31] Brazil First Written Submission, para. 158.

5.29 Furthermore, the United States claims that a substantial number of producers would not be affected by a reduction or elimination of payments because they plant on farms with no base acres or plant in excess of a farm's base acres[32], presents only part of the picture. While base acre yields are the basis for determining eligibility for counter-cyclical payments, they are irrelevant for determining marketing loan payments. So the producers who the United States claims would not be affected by the reduction or elimination of payments would in fact miss out on marketing loan payments if they were reduced or eliminated.

4. The Reliability of the Econometric Modelling

5.30 The United States claims that the econometric modelling provided by Brazil is flawed, but the United States arguments are either an attempt to reargue what was litigated before the original panel and the Appellate Body and lost, or are inconsequential. New Zealand will offer a few observations on the United States claims in this regard.

5.31 The United States makes much of the fact that in his new model Dr. Sumner has increased his United States cotton supply elasticity to 0.8.[33] However, as an alternative model to capture long run effects the United States proposes the ATPSM model which also has a United States cotton supply elasticity of 0.8![34] Moreover, the United States conveniently ignores footnote 301 in Brazil's submission[35] where it is stated "Brazil notes that Professor Sumner also ran 12 simulations using an even more conservative supply elasticity of 0.5. The results of this exercise demonstrate the robustness of the supply and price effects…."

5.32 The United States criticises Dr. Sumner for making a small change to the rest of the world (ROW) demand elasticity, -0.2 as opposed to -0.25. But this 0.05 change is a small change in relation to the alternatives that the United States then offers, i.e. a range of 0.45 between different scenarios.[36] How can the United States claim that its own estimates have a more solid statistical basis than those used by Dr. Sumner? In fact, Dr. Sumner's demand elasticities are little different from those he used in the earlier proceeding, which were implicitly found to be credible by the original panel and Appellate Body.

5.33 Although the United States notes that the coupling factor used by Dr. Sumner is the same as the one he used in his original model[37], it then goes on to criticize the size of that factor. Once again, the United States is attempting to relitigate what had already been found to be credible by both the panel and Appellate Body in the original proceeding. In any event, while the price effects are not enormous under the United States parameters, the effect on exports - especially in the long-term – certainly is.

5. Increase in the World Market Share

5.34 The United States contests Brazil's claim that the effect of the marketing loan and counter-cyclical payments programmes is to increase the United States world market share in upland cotton and hence constitutes serious prejudice within the meaning of Article 6.3(d) of the SCM Agreement. But in seeking to show that there has been no increase in United States market share, the United States is once again addressing the wrong question.

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[32] United States First Written Submission, para 298.

[33] Brazil First Written Submission, Annex I, paras. 10-21.

[34] United States First Written Submission, Annex I, Table A7.

[35] Brazil First Written Submission, para. 171.

[36] The ROW demand elasticities used by the United States range from -0.39 to -0.84. United States First Written Submission, Annex I, Table A7.

[37] United States First Written Submission, Annex I, para. 31.

5.35 The essence of Brazil's argument is that the United States market share is higher than it would otherwise be and that this is because of the marketing loan and counter-cyclical payments programmes. Thus, the United States arguments that its market share has not increased over the period in question are simply not relevant. Moreover, the United States own analysis proves Brazil's point. In its critique of Dr. Sumner's analysis, the United States indicates that the long-term effect of the elimination of marketing loan and counter-cyclical payments would be a reduction in United States cotton exports of up to 25 per cent in 2002-2005 and 17 per cent in 2006-2008.[38] That is a very clear measure of what United States world market share would be in the absence of the marketing loan and counter-cyclical payments programmes.

5.36 In short, the United States itself makes the *prima facie* case under Article 6.3(d) of the SCM Agreement that it claims that Brazil has been unable to make.

VI. CONCLUSION

6.01 In conclusion, in New Zealand's view, Brazil has demonstrated that the United States has failed either to withdraw the marketing loan and counter-cyclical payments programmes or to remove the adverse effects of those programmes as required by Article 7.8 of the SCM Agreement. Accordingly, the United States has failed to comply with the recommendations and rulings of the DSB of 21 March 2005.

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[38] United States First Written Submission, Annex I, Table A8.