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Negotiating Group on Rules

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TREATMENT OF GOVERNMENT SUPPORT FOR EXPORT CREDITS AND GUARANTEES UNDER THE AGREEMENT ON SUBSIDIES AND COUNTERVAILING MEASURES

Paper from Brazil

The following communication, dated 31 March 2005, is being circulated at the request of the Delegation of Brazil.

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1. Brazil supplements its communication dated 25 April 2002 (TN/RL/W/5), to further explain its views and propose specific new language for Items (j) and (k) of Annex I of the *Agreement on Subsidies and Countervailing Measures* (ASCM) to avoid any negative impact on developing country Members of the WTO.

2. Brazil's proposals have the aim of clarifying the provisions addressed and making them unambiguous. These proposals should not be construed as signifying that the rights and obligations they make explicit are not already contained in the provisions in their current ASCM formulation.

Items (j) and (k)

3. Brazil's concerns regarding Items (j) and (k) can be divided into two basic categories: (i) procedural fairness and sovereignty; and (ii) the substance of Item (j) and (k) and the relationship of the ASCM (*via* Item (k)) to the *Arrangement on Guidelines for Officially Supported Exported Credits* ("Arrangement"), whose participants are all the members of the Organization for Economic Cooperation and Development (OECD).

Procedural Fairness and Sovereignty

4. Paragraph 2 of Item (k) of Annex I of the ASCM refers to, and incorporates by reference, interest rates provisions of the Arrangement. Item (k) creates a safe harbour for the grant of government export credits in conformity with the interest rate provisions of the Arrangement. WTO panel reports have interpreted Item (k) as referring not to the interest rate provisions of the Arrangement as they existed at the conclusion of the Uruguay Round, but to whatever version of the Arrangement is in force at the time the financing support is offered.

5. This so-called "evolutionary interpretation" raises profound systemic concerns regarding procedural fairness and sovereignty, as not all WTO Members are Participants to the Arrangement ("Participants").

6. Non Participants do not vote, take part in discussions or even review or have advance notice of decisions taken in that forum.

7. Thus, for non-Participants to be subject to Arrangement rules *via* Item (k) evinces a patent lack of fairness that should not be countenanced in a multilateral trade regime ostensibly devoted to establishing a level playing field among all WTO Members.

8. Moreover, this aspect of the ASCM represents an unacceptable encroachment on the sovereignty of non-Participants that cannot be bound by rules established by any procedure short of a consensus of all WTO Members.

9. To be sure, Members of the WTO (as a whole) have the right to select a set of rules to refer to for the purpose of creating a safe harbour for government grants of permissible export credits. Under no circumstances, however, should a small group of WTO Members be allowed to change those rules through decisions taken in another forum. Any renunciation of sovereignty by the Members of the WTO must be explicit and unambiguous, in accordance with customary rules of public international law.

10. In other words, a minority of WTO Members must never be allowed to unilaterally to change the rules that have been negotiated and agreed to by all WTO Members. This aspect of the current ASCM must be clarified, so as to avoid mistaken interpretations such as those adopted by the above mentioned panels (see proposed language below).

<u>The Substance of Items (j) and (k) and Proposed New Text</u>

11. The substantive concerns raised by Items (j) and (k) and by the relationship between the ASCM (*via* Item (k)) and the Arrangement are also important. The fundamental concern is that Items (j) and (k) favour countries with lower perceived risk (i.e. developed countries), to the disadvantage of countries with higher risk (e.g. developing countries). Unfortunately, Items (j) and (k) tilt further in favour of the developed countries a playing field – the provision of guarantees and financing for sales – in which these countries already hold a significant advantage.

<u>Item (j)</u>

12. Item (j) prohibits governments from providing export credit guarantee or insurance programmes (or other specified risk guarantees) at premium rates that are inadequate to cover "long-term operating costs and losses of the programmes". The net effect of some interpretations of this provision is to provide developed countries a much larger safe harbour than is provided to developing countries. This is due to the fact that developed countries generally have higher credit ratings than developing countries. Based on their higher credit ratings, developed countries are able to provide export credit guarantees or insurance programmes that lower the overall interest rate to below market levels, if compared to the overall interest rate offered by international capital markets without the cited guarantee.

13. This safe harbour institutionalizes a bias in favour of developed country Members of the WTO at the expense of developing country Members.

14. To remedy these problems, Brazil proposes new text for Item (j), as follows:

> "(j) The provision by governments (or special institutions controlled by governments) of export credit guarantee or insurance programmes, of insurance or guarantee programmes against increases in the cost of exported products or of exchange risk programmes, at premium rates which are inadequate to cover either: (i) the long term operating costs and losses of the programmes or (ii) the difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by the government and the amount that the firm would pay on a comparable commercial loan absent the government guarantee."

15. The net effect of the new language at the end of proposed Item (j) would be to help establish a level playing field for all WTO Members regarding the provision of export credit guarantees or insurance programmes. The added language would include in the illustrative list, for the sake of clarity, the practice where developed countries provide guarantees at rates that are so low that the overall interest rate is below market, thus conferring a benefit as measured in Article 14(c) of the ASCM.

Item (k)

16. Item (k) raises similar concerns. One of the biggest disadvantages of developing countries *vis-à-vis* developed countries relates to financing for sales of large capital goods. The cost of capital for developing countries is higher than that for developed countries, due primarily to perceived risk. First paragraph of Item (k) ties each Member to its cost of capital, precluding negotiation of more competitive rates, such as those offered by Members with lower cost of funds. This aspect of the ASCM regime, therefore, creates a larger safe harbour for developed countries as opposed to developing countries.

17. As indicated above, the second paragraph of Item (k), in its current formulation, raises serious systemic concerns about procedural fairness and sovereignty.

18. To address these problems, Brazil proposes new text for Item (k) as follows:

> "(k) The grant by governments (or special institutions controlled by and/or acting under the authority of governments) of export credits at rates below those available on international capital markets (absent any government guarantee or support), for funds of the same maturity and other credit terms and denominated in the same currency as the export credit, or the payment by them of all or part of the costs incurred by exporters or financial institutions in obtaining credits, in so far as they are used to secure a material advantage in the field of export credit terms;
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> Provided, however, that if a Member is a party to an international undertaking on official export credits to which at least twelve original Members to this Agreement are parties as of 1 January 1979, or if in practice a Member applies the interest rates 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. For purposes of this provision, the relevant text of the international undertaking shall be the text in effect as at the conclusion of the Uruguay Round, unless WTO Members by consensus adopt a subsequent version thereof."

19. The changes suggested in the first paragraph would ensure that export credits are not supplied at rates below market level. In the second paragraph, the final sentence would clarify that the 1992 Arrangement, and not any of its subsequent versions, is the "international undertaking" used to determine whether Member-provided export credits fall within the safe harbour, unless WTO Members, by consensus, agree otherwise.

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