

**CANADA – EXPORT CREDITS AND
LOAN GUARANTEES FOR REGIONAL AIRCRAFT**

Report of the Panel

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I. INTRODUCTION

A. COMPLAINT OF BRAZIL

1.1 On 22 January 2001, Brazil requested consultations¹ with Canada pursuant to Article XXIII:1 of the General Agreement on Tariffs and Trade 1994 ("GATT 1994"), Article 4 of the Understanding on Rules and Procedures Governing the Settlement of Disputes ("DSU"), and Article 4 of the Agreement on Subsidies and Countervailing Measures ("SCM Agreement") regarding certain alleged subsidies granted by the Government of Canada and the Province of Québec that support the export of regional aircraft from Canada.

1.2 Brazil and Canada held consultations on 21 February 2001, but failed to reach a mutually satisfactory solution.

1.3 On 1 March 2001, Brazil requested the establishment of a panel pursuant to Article XXIII of the GATT 1994, Article 6 of the DSU, and Article 4.4 of the SCM Agreement.²

B. ESTABLISHMENT AND COMPOSITION OF THE PANEL

1.4 The Dispute Settlement Body ("DSB") established a panel on 12 March 2001, with standard terms of reference. The terms of reference of the Panel are:

To examine, in the light of the relevant provisions of the covered agreements cited by Brazil in document WT/DS222/2, the matter referred to the DSB by Brazil in that document, and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements.

1.5 On 7 May 2001, Brazil requested the Director-General to determine the composition of the Panel, pursuant to paragraph 7 of Article 8 of the DSU. This paragraph provides:

If there is no agreement on the panelists within 20 days after the date of the establishment of a panel, at the request of either party, the Director-General, in consultation with the Chairman of the DSB and the Chairman of the relevant Council or Committee, shall determine the composition of the panel by appointing the panelists whom the Director-General considers most appropriate in accordance with any relevant special or additional rules or procedures of the covered agreement or covered agreements which are at issue in the dispute, after consulting with the parties to the dispute. The Chairman of the DSB shall inform the Members of the composition of the panel thus formed no later than 10 days after the date the Chairman receives such a request.³

¹ See WT/DS222/1.

² See WT/DS222/2.

³ Paragraph 12 of Article 4 of the SCM Agreement provides:

For purposes of disputes conducted pursuant to this Article, except for time-periods specifically prescribed in this Article, time-periods applicable under the DSU for the conduct of such disputes shall be half the time prescribed therein.

1.6 On 11 May 2001, the Director-General accordingly composed the panel as follows:

Chairman: Prof. William J. Davey
Members: Prof. Seung Wha Chang
Ms. Usha Dwarka-Canabady

1.7 Australia, the European Communities, India, and the United States reserved their rights to participate in the panel proceedings as third parties.

C. PANEL PROCEEDINGS

1.8 The Panel met with the parties on 27 and 28 June 2001, and on 31 July 2001. The Panel met with the third parties on 27 June 2001.

1.9 The Panel submitted its interim report to the parties on 19 October 2001. Comments from the parties on the interim report were received on 26 October 2001, and on each other's comments on 2 November 2001 (*See* Section VI, *infra*). The Panel submitted its final report to the parties on 9 November 2001.

II. FACTUAL ASPECTS

2.1 This dispute concerns various Canadian measures which Brazil alleges are subsidies inconsistent with Canada's obligations under Article 3.1(a)⁴ of the SCM Agreement in that they are contingent in law or in fact, whether solely or as one of several other conditions, upon export performance.⁵

2.2 The measures as identified in Brazil's request for the establishment of a panel are export credits, including financing, loan guarantees, or interest rate support provided by or through the Export Development Corporation ("EDC") – both Canada and Corporate Accounts thereunder – to facilitate the export of civil aircraft, and export credits and guarantees, including loan guarantees, equity guarantees, residual value guarantees, and "first loss deficiency guarantees", provided by *Investissement Québec* ("IQ"), a programme operated by the Province of Québec.

III. PARTIES' REQUESTS FOR FINDINGS AND RECOMMENDATIONS

A. BRAZIL

3.1 In its request for establishment, Brazil requests that the panel find that:

1. Export credits, including financing, loan guarantees, or interest rate support by or through the Canada Account are and continue to be prohibited export subsidies within the meaning of Articles 1 and 3 of the SCM Agreement.
2. Canada has not implemented the report of the Article 21.5 panel, adopted by the DSB, requesting that Canada withdraw Canada Account subsidies.
3. Canada, in defiance of the rulings and recommendations of the Dispute Settlement Body, continues to grant or offers to grant export credits to the regional aircraft industry through the

⁴ We understand Brazil's reference in its request for the establishment of a panel to Article 3 of the SCM Agreement to mean Article 3.1(a) of the Agreement.

⁵ *See* footnote 14, *infra*.

Canada Account, that are prohibited subsidies within the meaning of Articles 1 and 3 of the Agreement.

4. Canada's grant or offer to grant Canada Account export credits to Air Wisconsin is a prohibited export subsidy within the meaning of Articles 1 and 3 of the Agreement.
5. Export credits, including financing, loan guarantees, or interest rate support by or through the EDC are prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.
6. Canada's grant or offer to grant export credits by or through EDC to Air Wisconsin is a prohibited export subsidy within the meaning of Articles 1 and 3 of the Agreement.
7. Export credits and guarantees provided by *Investissement Québec*, including loan guarantees, equity guarantees, residual value guarantees, and "first loss deficiency guarantees" are prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.⁶

3.2 Brazil further requested that the Panel recommend that the DSB direct Canada to withdraw these prohibited subsidies without delay.⁷

B. CANADA

3.3 Canada requests that the Panel find that Brazil has failed to present a *prima facie* case that any of the Canada Account, Corporate Account or *IQ* programmes, "as such", "as applied" or in respect of "specific transactions" are inconsistent with Canada's obligations under the SCM Agreement.⁸

3.4 Canada considers that:

1. There is no basis for this Panel to reverse the findings in *Canada – Aircraft*⁹ that EDC (Corporate Account) and Canada Account are discretionary;
2. *IQ* is not "as such" inconsistent with the SCM Agreement;
3. Brazil's "as such" claims would improperly condemn all ECAs, and are at odds with the facts and the law;
4. Brazil seeks to make an untenable distinction between its challenges to measures "as applied" and in respect of "specific transactions"; and
5. Brazil has failed to show that any specific transactions, under Corporate Account, *IQ* or Canada Account, including Air Wisconsin, are inconsistent with Canada's obligations under the SCM Agreement, because they are not inconsistent.

IV. ARGUMENTS OF THE PARTIES

4.1 The arguments of the parties are set out in their submissions to the Panel. The parties' submissions are attached to this Report as Annexes (*See* List of Annexes, page v).

⁶ WT/DS222/2.

⁷ *Id.*

⁸ Canada also raises a number of preliminary objections in respect of the claims of Brazil. *See* para. 7.3, *infra*.

⁹ *Canada – Measures Affecting the Export of Civilian Aircraft* ("*Canada – Aircraft*"), Report of the Panel, WT/DS70/R, and Report of the Appellate Body, WT/DS70/AB/R, adopted 20 August 1999.

V. ARGUMENTS OF THE THIRD PARTIES

5.1 The arguments of the third parties – Australia, the European Communities, India, and the United States – are set out in their submissions to the Panel and are attached to this Report as Annexes (*See* List of Annexes, page v).

VI. INTERIM REVIEW

6.1 On 26 October 2001, both parties submitted written requests for review by the Panel of particular aspects of the interim report issued on 19 October 2001. On 2 November 2001, each party provided written comments on certain aspects of the other party's request for interim review. Neither party requested an additional meeting with the Panel. The issues raised by the parties are addressed below. The Panel deleted paragraph 7.263 of the interim report, and made minor changes to paragraphs 7.243, 7.256, 7.259, 7.262, 7.276, and 7.284 of the interim report.

A. BRAZIL'S REQUEST FOR INTERIM REVIEW

6.2 Brazil drew the attention of the Panel to a number of typographical and factual errors in the interim report, which we have corrected.

6.3 Brazil requested a change to the Panel's description of Brazil's argument in paragraph 7.221 of the interim report. Canada denied the need for any such change. In order to avoid any misunderstanding, we have deleted that paragraph from the final version of our report.

6.4 Brazil requested the inclusion of a note to paragraph 7.226 of the interim report, to the effect that Brazil was able to obtain details of Embraer's offer to Air Wisconsin. Canada objected to the note requested by Brazil, in part because Brazil obtained those details in response to a direct request from the Panel. In our view, the fact that Brazil was able to obtain details of an offer made by Embraer in response to a request from the Panel has no bearing on the issue of whether or not it would be realistic to expect the EDC to have access to data regarding commercial financing transactions involving Bombardier aircraft. We therefore decline to include the note requested by Brazil.

6.5 With regard to note 278 of the interim report, Brazil relies on Exhibit CAN-61 to suggest that CQC participated in the Midway transaction as an equity investor. In response, Canada asserted that "[n]either IQ nor CQC were equity participants in the Midway transaction". Canada also confirmed the factual accuracy of note 278 of the interim report. In light of Canada's response, we have not made any changes to note 278 of the interim report.

B. CANADA'S REQUEST FOR INTERIM REVIEW

6.6 Canada drew the attention of the Panel to a number of typographical and factual errors in the interim report. In some cases we have corrected the error. In other cases we have made deletions.

6.7 Canada objects to the Panel's statement in para. 7.18 of the interim report that "the legal framework under which the Canada Account is operated has changed", indicating that it has not and referring to Canada's oral response to that effect to a question by the Panel at the second meeting with the parties. Brazil asserts that the legal framework under which the Canada Account operates has changed.

6.8 The Panel makes the relevant statement in the context of its assessment of Canada's request for a preliminary ruling under Article 21.5 of the DSU in respect of Brazil's Claims 1 and 3. The basis for the Panel's statement is that, following the *Canada – Aircraft* panel's decision, Canada enacted the

*Policy Directive GEN 000-004 – Submission of Documents to the Government of Canada*¹⁰ and the *EDC Canada Account Policy Guideline*¹¹, which require Canada Account financing to comply with the OECD Arrangement (*See* paragraph 7.93, *infra*). We note also that Brazil disagrees with Canada's objection, pointing to the policy memorandum enacted by Canada following the first *Canada – Aircraft* dispute. Accordingly, we retain the statement in para. 7.18 of the interim report, and have included note 21 in the final report for clarification.

6.9 Canada requested a change to the Panel's description of its argument in the last sentence of paragraph 7.145 of the interim report. Brazil has objected to the change requested by Canada. Since we do not consider that the current version is inaccurate in any way, we decline to make the change requested by Canada.

6.10 Canada questioned the factual accuracy of a statement made by the Panel in the third sentence of paragraphs 7.152 and 7.316 of the interim report. Brazil objected to the concern raised by Canada, largely because Canada failed to make the relevant argument during the substantive part of the proceedings. In order to avoid any factual error in our findings, we have deleted the third sentence of paragraphs 7.152 and 7.316 of the interim report.

6.11 With regard to paragraph 7.247 of the interim report, Canada objected to the Panel's addition of 20-30 basis points to large aircraft EETC spreads to arrive at an appropriate regional aircraft spread. The Panel made this adjustment in response to Brazil's reliance on statements made by Canada in the *Brazil – Aircraft – Second 21.5* proceedings (*See* paragraphs 47 and 50 of Oral Statement of Brazil at the Second Meeting of the Panel (Annex A-12)). In responding to Brazil's oral statement¹², Canada made no attempt to deny the need for a 20-30 basis point adjustment when converting from large aircraft to regional aircraft spreads. Nor did Canada object to Brazil's inclusion of a 20 basis point adjustment ("for the difference between the regional aircraft used in the financing at issue and the larger jets used in the typical EETC issue") in its Exhibit BRA-66. Furthermore, although Canada asserts that "[v]ariations in pricing between similar but non-identical asset classes are dynamic and subject to change ...", Canada does not deny the need for an adjustment *per se*. However, although Canada appears to accept the need for an adjustment of some sort, Canada fails to indicate what would be, in its view, an appropriate adjustment for the transactions at issue. In addition, we note that a lesser adjustment would not necessarily change the outcome of our findings. For these reasons, we see no need to change paragraph 7.247 of the interim report.

6.12 Regarding paragraph 7.255 of the interim report, Canada made a number of arguments as to why FMC data could be used to assess transactions in certain circumstances. In doing so, however, Canada "does not [] reject Brazil's observation that the FMC represents an average of current pricing levels of the bonds of a wide range of similarly rated companies". Since it is the inclusion of average data that caused the Panel not to base its findings on FMC data, and since Canada has not denied that average data were included, we make no changes to paragraph 7.255 of the interim report.

6.13 In respect of paragraph 7.276 of the interim report, Canada asserted that the Panel should not have concluded that EDC financing [] does not include an []. Canada submits that the fixed margin for credit risk [] on the authority of the President or Senior Vice President Finance and Chief Financial Officer of the EDC. According to Canada, "an authorized margin [] the identified fixed margin is [] for that transaction". Brazil objected to any change to paragraph 7.276 of the interim report.

¹⁰ Exhibit CAN-16.

¹¹ Exhibit CAN-17.

¹² *See* Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel (Annex B-12).

6.14 We note that the EDC offered financing [] to Comair in two instances: in July 1996 and August 1997. Canada submitted EDC Pricing Documentation regarding these offers in the form of Exhibit CAN-59. This exhibit does not contain any details regarding the basis on which the President or Senior Vice President Finance and Chief Financial Officer of the EDC may have authorised [] the fixed margin for credit risk. Nor does it contain any data indicating that any margin authorised by the President or Senior Vice President Finance and Chief Financial Officer of the EDC was [] for the two transactions at issue. For these reasons, we reject Canada's assertion that the Panel should not have concluded that the relevant EDC financing [] does not include [].

VII. FINDINGS

A. INTRODUCTION

7.1 This dispute concerns export credits, including financing, loan guarantees, or interest rate support provided by or through the Canada-owned EDC – both Canada and Corporate Accounts thereunder – to facilitate the export of civil aircraft as well as export credits and guarantees, including loan guarantees, equity guarantees, residual value guarantees, and "first loss deficiency guarantees", provided by *IQ*, a programme operated by the Province of Québec. Brazil claims that the EDC and *IQ* programmes "as such" and "as applied" are prohibited export subsidies, in violation of Article 3.1(a)¹³ of the SCM Agreement. Brazil also claims that specific transactions under those programmes constitute prohibited export subsidies.¹⁴

7.2 After addressing certain preliminary issues raised by Canada, we shall begin our substantive review by examining Brazil's claims regarding the EDC programmes "as such" and "as applied". We shall then turn to Brazil's claims regarding specific transactions under those programmes. In examining specific transactions, we shall first review Brazil's claims regarding EDC support to Air Wisconsin. We shall then address Brazil's claims regarding other EDC support, before turning to Brazil's claims regarding support provided by *IQ*.

B. PRELIMINARY ISSUES

7.3 Canada raises the following preliminary objections in respect of the claims of Brazil:

1. Claims 1, 2, and 3 raise issues of compliance or implementation related to another dispute. These claims are inconsistent with Article 21.5 of the DSU. This panel does not have the jurisdiction to examine compliance issues that have arisen in other disputes; and

¹³ As noted above, we understand Brazil's reference in its request for the establishment of a panel to Article 3 of the SCM Agreement to mean Article 3.1(a) of the Agreement.

¹⁴ The Panel asked Brazil to "identify the specific measures in respect of which Brazil is requesting the Panel to make findings. In particular, is Brazil requesting findings (1) on the Canada Account, EDC and *IQ* programmes as such, (2) on the Canada Account, EDC and *IQ* programmes as applied (on the basis of evidence regarding specific transactions), (3) on the specific Canada Account, EDC and *IQ* transactions identified in its first submission, or (4) on some combination of (1), (2) and (3)?" Brazil replied that it "is requesting findings by the Panel on points (1), (2), and (3). Brazil is requesting that the Panel find the Canada Account, EDC and *IQ* programmes as such inconsistent with Canada's obligations under the SCM Agreement. Brazil is also requesting that the Panel find the Canada Account, EDC and *IQ* programmes inconsistent with Canada's obligations under the SCM Agreement as applied on the basis of evidence regarding specific transactions. Finally, Brazil is requesting that the Panel find the specific Canada Account, EDC and *IQ* transactions identified in its First Written Submission as breaching Canada's obligations under the SCM Agreement" (Response of Brazil to Question 25 from the Panel, Responses of Brazil to Questions from the Panel Following the First Meeting of the Panel (Annex A-9)).

2. Claims 1, 2, 5, and 7 are inconsistent with the requirements of Article 6.2 of the DSU, which require a complaining party to identify the specific matters at issue and to provide a brief summary of the legal basis of the complaint, sufficient to present the problem clearly. Brazil has not met the minimum standards of this provision.

1. Disputes over implementation – Article 21.5 of the DSU (regarding claims 1, 2, and 3 of Brazil)

(a) Arguments of the parties

(i) *Canada*

7.4 Canada argues that the DSU provides that disputes over implementation are to be resolved through expedited proceedings provided for in Article 21.5, rather than through new panel proceedings. Canada further points out that Article 21.5 uses mandatory, not hortatory, language. Where there is disagreement over implementation, such a dispute "shall be decided through recourse to these dispute settlement procedures, including wherever possible resort to the original panel". Canada submits that, in all cases to date in which there has been a dispute over the existence or WTO-consistency of measures taken to comply with DSB recommendations or rulings, resort has been had to Article 21.5. In Canada's view, to allow a Member to ignore the specific requirements of Article 21.5 and instead to resort to *de novo* panel proceedings to determine issues of implementation would be contrary to Article 21.5. Moreover, any panel established through the regular dispute settlement procedures of Article 6 of the DSU would not have the jurisdiction to make findings on issues of compliance arising from other cases.

Claim 1

7.5 Canada recalls that Claim 1 states:

Export credits, including financing, loan guarantees, or interest rate support by or through the Canada Account are and continue to be prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.

7.6 Canada points out that, in this claim, Brazil asserts in part that certain export credits "continue to be" prohibited export subsidies. Canada argues that all measures of a Member are presumed to be WTO-consistent absent a specific DSB ruling to the contrary. Therefore, the reference by Brazil to export credits that "continue to be" prohibited export subsidies must refer back to earlier DSB rulings that certain "export credits" granted by Canada are not WTO-consistent. According to Canada, this would appear to be a claim that Canada has not complied with the DSB rulings in *Canada – Aircraft*. Canada argues that this panel does not have the jurisdiction to determine issues of compliance related to other cases.

Claim 2

7.7 Canada recalls that Claim 2 states:

Canada has not implemented the report of the Article 21.5 panel, adopted by the DSB, requesting that Canada withdraw Canada Account subsidies.

7.8 Canada submits that Claim 2 fails to specify which "report of the Article 21.5 panel" is the subject of the current Brazilian complaint. Canada presumes that it is the report of the Article 21.5 panel in *Canada – Measures Affecting the Export of Civilian Aircraft* ("*Canada – Aircraft*"). In any event, argues Canada, a complaint that Canada "has not implemented" the Article 21.5 panel report is clearly

an issue of compliance or implementation related to an earlier dispute, which is outside the jurisdiction of the present panel.

Claim 3

7.9 Canada recalls that Claim 3 provides:

Canada, in defiance of the rulings and recommendations of the Dispute Settlement Body, continues to grant or offers to grant export credits to the regional aircraft industry through the Canada Account, that are prohibited subsidies within the meaning of Articles 1 and 3 of the Agreement.

7.10 Once again, argues Canada, Brazil has referred to "the rulings and recommendations of the Dispute Settlement Body", without any reference as to which such rulings or recommendations are the subject of the current complaint. Again, Canada surmises that Brazil is referring to the rulings and recommendations of the DSB in *Canada – Aircraft*. The reference to the alleged granting of, or offers to grant, prohibited subsidies "in defiance of" the DSB rulings clearly indicates, in the opinion of Canada, that this claim raises issues of compliance with earlier rulings. Such claims are outside the jurisdiction of the current panel according to Canada.

(ii) *Brazil*

7.11 Brazil disagrees that it cannot challenge, in proceedings brought pursuant to Article 6 of the DSU, the existence or consistency of measures taken to comply with the earlier recommendations and rulings of the DSB with respect to the Canada Account. While it is the case, in the view of Brazil, that a Member may challenge under Article 21.5 "measures taken to comply" with DSB recommendations and rulings, the ordinary meaning of Article 6.2 of the DSU and Articles 4.1, 4.4, and 4.5 of the SCM Agreement do not preclude a Member from similarly bringing a new dispute settlement proceeding under those provisions. Brazil argues that, if a Member chooses to forego the expedited procedures under Article 21.5, it is its prerogative to do so, and requiring Members to avail themselves of only those expedited procedures would be contrary to the object and purpose of Article 21.5. Brazil further posits that, in the circumstances of this particular case, it "considered it efficient to forego Article 21.5's expedited procedures"¹⁵, as Brazil's challenge to Canada Account support for regional aircraft involves claims against the measure both as such and as applied in particular transactions, and a panel constituted under Article 21.5 would not be authorised to review the consistency of Canada Account support as applied in particular regional aircraft transactions.

7.12 Further, Brazil considers that Canada is incorrect to identify each of the numbered paragraphs regarding the Canada Account in Brazil's request for the establishment of a panel as a separate claim. Brazil submits that it makes one overarching claim with respect to Canada Account support in its request for establishment, in paragraph 1. Paragraphs 2-4 of the request explain the nature of that claim, according to Brazil.

7.13 Brazil submits that the *Canada – Aircraft* panel did not rule that Canada Account as such was consistent with the SCM Agreement. It found that Brazil had failed to make a *prima facie* case and, as a result, the Panel could not "make any findings on the Canada Account programme *per se*."¹⁶ With respect to Canada Account, Brazil argues that it has now presented additional information and evidence that presents a *prima facie* case.

¹⁵ Response of Brazil to Submission of Canada Regarding Jurisdictional Issues, para. 8 (Annex A-4).

¹⁶ *Canada – Aircraft*, Report of the Panel, footnote 9, *supra*, para. 9.213.

(b) Evaluation by the Panel

(i) *Claims 1 and 3*

7.14 We recall that Claims 1 and 3 read as follows:

Claim 1

Export credits, including financing, loan guarantees, or interest rate support by or through the Canada Account are and continue to be prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.

Claim 3

Canada, in defiance of the rulings and recommendations of the Dispute Settlement Body, continues to grant or offers to grant export credits to the regional aircraft industry through the Canada Account, that are prohibited subsidies within the meaning of Articles 1 and 3 of the Agreement.

7.15 In essence, Canada argues that Claims 1 and 3 are claims related to the implementation of the DSB recommendations in *Canada – Aircraft*, and that this panel does not have the jurisdiction to determine issues of compliance related to other cases. In our view, however, the use of the words "continue to be" and "in defiance of the rulings and recommendations of the [DSB]" do not necessarily indicate that what is sought by Brazil is a review of "measures taken to comply with" the DSB recommendations, as that term is used in Article 21.5 of the DSU. Indeed, Brazil, in its response to our question, submits that it "is not asking this Panel to review the findings of the DS70 Article 21.5 Panel or to uphold or confirm the findings of that Panel. Similarly, Brazil is not asking this Panel to draw conclusions as to what Canada should have done." Thus, in our view, the present panel has not been asked to rule on whether Canada implemented the DSB recommendations in the *Canada – Aircraft* case.

7.16 In our view, the wording of both Claims 1 and 3 alleges current violations of Article 3.1(a) of the SCM Agreement, which sets out the prohibition on export subsidies and reads as follows:

subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I (footnotes deleted);

To prove the existence of an export subsidy within the meaning of this provision, a Member must therefore establish (i) the existence of a subsidy within the meaning of Article 1 of the SCM Agreement and (ii) contingency of that subsidy upon export performance. It is these elements that must be set out for purposes of a claim under Article 3.1(a). In this regard, we consider that the phrases "continue to be" and "in defiance of the rulings and recommendations of the [DSB]" – which form the basis for Canada's preliminary objection in respect of Claims 1 and 3 – are surplus. What Brazil must prove to carry its Article 3.1(a) claims are the elements necessary under that provision. In our view, the above phrases used by Brazil in its request for establishment and subsequently cited by Canada are simply not relevant to Brazil's claims under Article 3.1(a). Accordingly, our focus must be on whether Brazil has set out the elements necessary under Article 3.1(a), and that is what we shall address.

7.17 We note that, in respect of Claims 1 and 3, Brazil states that "Brazil simply is requesting a factual finding that, since the adoption of the DS70 Article 21.5 Report, Canada has not made any

changes in Canada Account"¹⁷. With regard to this "factual finding" requested by Brazil, we recall that Article 11 of the DSU – which sets out the function of panels – states in relevant part:

The function of panels is to assist the DSB in discharging its responsibilities under this Understanding and the covered agreements. Accordingly, a panel should make *an objective assessment of the matter before it, including an objective assessment of the facts of the case and the applicability of and conformity with the relevant covered agreements*, and make such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the covered agreements (emphasis added).

We further note that the terms of reference of this panel are:

To examine, in the light of the relevant provisions of the covered agreements cited by Brazil in document WT/DS222/2, the matter referred to the DSB by Brazil in that document, and to make such findings as will assist the DSB in making the recommendations or in giving the rulings provided for in those agreements.

We do not consider that the "factual finding" requested by Brazil is a "matter" we should objectively assess or examine in this case. It is simply not relevant to whether Brazil has established its Article 3.1(a) claims in this proceeding, which we consider to be "such other findings as will assist the DSB in making the recommendations or in giving the rulings provided for in the [SCM Agreement]".¹⁸

7.18 Finally, we note that, whether or not the phrases "and continue to be" and "in defiance of the rulings and recommendations of the [DSB]" are viewed as irrelevant surplus in respect of Claims 1 and 3, we view the claims in this proceeding to be different and broader than those that were the subject of the *Canada – Aircraft* ruling. The *Canada – Aircraft* panel held that "the Canada Account debt financing at issue constitutes 'subsid[ies] contingent in law . . . upon export performance' prohibited by Article 3.1(a) of the SCM Agreement"¹⁹. The Panel had found that "the Canada Account debt financing in issue takes the form of export credits"²⁰. Claims 1 and 3 of Brazil are made, respectively, in relation to "[e]xport credits, including financing, loan guarantees, or interest rate support, by or through the Canada Account" and "export credits . . . through the Canada Account". Brazil's claims in this proceeding do not concern the specific financing transactions "at issue" in the *Canada – Aircraft* case. Rather, different transactions are at issue. Moreover, the legal framework under which the Canada Account is operated has changed, as noted below.²¹ The scope of the *Canada – Aircraft* ruling is therefore different and narrower than that of the ruling requested of the present panel.

7.19 For the foregoing reasons, we reject Canada's objection to Claims 1 and 3.

(ii) *Claim 2*

¹⁷ Response of Brazil to Question 27 from the Panel, Responses of Brazil to Questions from the Panel Following the First Meeting of the Panel (Annex A-9).

¹⁸ Brazil's request for a factual finding seems to be based on Claim 2, which we find is not within our terms of reference (*See* paras. 7.45-7.49, *infra*). To the extent that it might also be based on other claims of Brazil, we address it as such.

¹⁹ *Canada – Aircraft*, Report of the Panel, footnote 9, *supra*, para. 9.231.

²⁰ *Id.*, para. 9.230.

²¹ In this regard, we note the fact that, following the ruling of the *Canada – Aircraft* panel, Canada enacted the *Policy Directive GEN 000-004 – Submission of Documents to the Government of Canada* (Exhibit CAN-16) and the *EDC Canada Account Policy Guideline* (Exhibit CAN-17), which require Canada Account financing to comply with the *OECD Arrangement* (*See* para. 7.93, *infra*).

7.20 We note that Canada has also requested a preliminary ruling under Article 6.2 in respect of Claim 2 (*See* paragraph 7.25, *infra*). In light of our ruling in that regard (*See* paragraph 7.49, *infra*), we need not, and do not, address Canada's request for a preliminary ruling under Article 21.5 in respect of Claim 2.

2. Specificity of the Request for the Establishment of a Panel – Article 6.2 of the DSU (regarding claims 1, 2, 5, and 7 of Brazil)

(a) Arguments of the parties

(i) *Canada*

7.21 Canada recalls that requests for the establishment of a panel must comply with the requirements of Article 6.2 of the DSU, which provides in part:

The request for the establishment of a panel . . . shall indicate whether consultations were held, identify the specific measures at issue and provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly.

7.22 Citing various Appellate Body statements, Canada emphasises the due process objective of Article 6.2 and submits that a deficiency in the request for the establishment of a panel cannot be cured by later submissions. Further, Canada recalls that, in determining whether Article 6.2 has been violated, panels and the Appellate Body have taken into account whether there has been prejudice to the rights of defence of the defending party during the course of the panel proceedings.

Claim 1

7.23 Canada recalls that Claim 1 states:

Export credits, including financing, loan guarantees, or interest rate support by or through the Canada Account are and continue to be prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.

7.24 Canada considers that the reference to "export credits" in Claim 1 is extremely broad. Any practice that allows payment to be deferred for an exported good or service could conceivably qualify as an "export credit" according to Canada. Moreover, argues Canada, the term "export credits" is limited neither to the Air Wisconsin transaction nor to the regional aircraft industry. The scope of "export credits", without any further clarification, is infinite. Brazil has failed to specify either the meaning or the scope of its claim. Further, Canada submits that the term "Canada Account" is not limited in any way in Brazil's claim. It is limited neither to the Air Wisconsin transaction nor to the regional aircraft industry. It appears to Canada from the terms of the claim that Brazil is challenging the whole of Canada Account, transactions under which number in the hundreds and vary from tied-aid transactions to insurance products.

Claim 2

7.25 Canada recalls that Claim 2 states:

Canada has not implemented the report of the Article 21.5 panel, adopted by the DSB, requesting that Canada withdraw Canada Account subsidies.

7.26 Canada indicates that, in Claim 2, Brazil has failed to identify any treaty provision that Canada is alleged to have violated. It makes no reference to any provision of the WTO Agreements. In the view of Canada, it thus fails to meet the "minimum prerequisite" of Article 6.2.

Claim 5

7.27 Canada recalls that Claim 5 states:

Export credits, including financing, loan guarantees, or interest rate support by or through the EDC are prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.

7.28 Canada makes the same argument in respect of the reference to "export credits" in Claim 5 as in Claim 1, that is, that the reference is extremely broad. Further, Canada considers that "Brazil's reference to 'the EDC' is similarly so broad as to defy definition"²². The term "EDC" in this claim, points out Canada, is limited neither to the Air Wisconsin transaction nor the regional aircraft industry. The claim appears to Canada to be an ill-defined attack on the whole of the EDC, a claim that could potentially cover hundreds of clients and many thousands of transactions since 1995.

Claim 7

7.29 Canada recalls that Claim 7 states:

Export credits and guarantees provided by *Investissement Québec*, including loan guarantees, equity guarantees, residual value guarantees, and "first loss deficiency guarantees" are prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.

7.30 Canada makes the same argument in respect of the reference to "export credits" in Claim 7 as in Claim 1, that is, that the reference is extremely broad. Further, Canada considers that the reference to "*Investissement Québec*" in Claim 7 is limited neither to the Air Wisconsin transaction nor to the regional aircraft industry.

7.31 In sum, Canada submits that it "does not know the violations Brazil is alleging and the case it has to answer"²³. In the opinion of Canada, Brazil's violations of the mandatory requirements of Article 6.2 of the DSU prejudice Canada's ability to prepare and present a full defence in this proceeding.

7.32 Canada considers Brazil's "overarching claim" theory an attempt to cure the deficiencies of Brazil's request for the establishment of a panel. Canada points out that Brazil did not request findings that Canada Account, Corporate Account, and *IQ* "as such, as applied, and in individual transactions" constitute prohibited export subsidies.²⁴ Canada also goes to some length to highlight differences between Brazil's request for establishment and statements in subsequent submissions, differences which, in Canada's view, demonstrate further the failure of Brazil to abide by the requirements of Article 6.2. Specifically, Canada argues that Brazil's request uses all-encompassing language and only in its response to Canada's preliminary submission has Brazil advised Canada that certain measures were not included.

²² Submission of Canada Regarding Jurisdictional Issues, para. 51 (Annex B-3).

²³ *Id.*, para. 44.

²⁴ Response of Canada to Question 5 from the Panel, Responses of Canada to Questions from the Panel Following the First Meeting of the Panel (Annex B-7).

(ii) *Brazil*

7.33 Brazil considers that its request for the establishment of a panel meets the four criteria set out by the Appellate Body in *Korea – Dairy*, that is, that the request must: (i) be in writing; (ii) indicate whether consultations were held; (iii) identify the specific measures at issue; and (iv) provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly²⁵.

7.34 Brazil argues that its request identifies the three Canadian programmes at issue and, for them, the specific categories of support subject to its challenge. Further, for Brazil, the request specifically not only covers challenges to these measures as such, but states clearly that it is also a challenge to the measures as applied in, for instance, the Air Wisconsin transaction. With regard to Canada's complaint that Brazil's claims are extremely broad, Brazil considers that it is a Member's prerogative to challenge any measure, no matter how broad, that it considers inconsistent with another Member's WTO obligations.

7.35 Brazil also recalls that it states expressly in paragraphs 1, 5, and 7 of its request for establishment that the measures at issue are prohibited export subsidies within the meaning of Articles 1 and 3 of the SCM Agreement.

7.36 Finally, Brazil submits that the "attendant circumstances" in this case demonstrate that Canada's ability to defend itself has not been prejudiced.

(b) Evaluation by the Panel

(i) *Claim 1*

7.37 We recall that Claim 1 states:

Export credits, including financing, loan guarantees, or interest rate support by or through the Canada Account are and continue to be prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.

7.38 Canada's request for a preliminary ruling in respect of Claim 1 is based on the breadth of the terms "export credits" and "Canada Account" in the request for the establishment of a panel as it relates to the requirements set out in Article 6.2. That provision reads, in relevant part:

The request for the establishment of a panel shall be made in writing. It shall indicate whether consultations were held, identify the specific measures at issue and provide a brief summary of the legal basis of the complaint sufficient to present the problem clearly.

We note that the request for the establishment of a panel was made in writing in the present dispute, and that the request indicates that consultations were held. What the parties disagree on with regard to Claim 1 is whether the request identifies the specific measures at issue, in that Canada considers Claim 1 too broad.

7.39 In *European Communities – Computer Equipment*, the Appellate Body was required to consider the specificity of the US panel request, which referred, *inter alia*, to "all types of LAN [Local Area Network] equipment". In doing so, the Appellate Body stated:

²⁵ *Korea – Definitive Safeguard Measure on Imports of Certain Dairy Products* ("Korea – Dairy"), Report of the Appellate Body, WT/DS98/AB/R, adopted 12 January 2000, para. 120.

LAN equipment and PCs with multimedia capacity are both generic terms. Whether these terms are sufficiently precise to "identify the specific measure at issue" under Article 6.2 of the DSU depends, in our view, upon whether they satisfy the purposes of the requirements of that provision.

In *European Communities – Bananas*, we stated that:

It is important that a panel request be sufficiently precise for two reasons: first, it often forms the basis for the terms of reference of the panel pursuant to Article 7 of the DSU; and, second, it informs the defending party and the third parties of the legal basis of the complaint.

The European Communities argues that the lack of precision of the term, LAN equipment, resulted in a violation of its right to due process which is implicit in the DSU. We note, however, that the European Communities does not contest that the term, LAN equipment, is a commercial term which is readily understandable in the trade.²⁶

7.40 In applying the analysis of the Appellate Body to this case, we find that the term "export credits", which has a definite meaning and is found in the Illustrative List of Export Subsidies contained in Annex I to the SCM Agreement, is "readily understandable" in the context of a dispute under Article 3.1(a) of the SCM Agreement. The term "export credits" is also explained by the language following the word "including" in Brazil's request for establishment, i. e., the examples set out by Brazil. We note, further, that it is quite clear from Brazil's request for consultations that the measures at issue were limited to Canada's regional aircraft industry²⁷. It is therefore difficult, considering these attendant circumstances, to accept that Canada could not know that the terms "export credits" and "Canada Account" were related in particular to the regional aircraft industry.

7.41 With regard to the comparison Canada makes between the language in Brazil's request for establishment and its response to Canada's preliminary submission, it is clear that Article 6.2 imposes certain requirements on the contents of a request for establishment, not on how these contents compare with subsequent articulations of the complainant's claims. We are of the view that such arguments by Canada, while perhaps illustrative, are not legally relevant to any assessment under Article 6.2.

7.42 Thus, in our view, Brazil's request for the establishment of a panel satisfies the requirement under Article 6.2 of the DSU to "identify the specific measures at issue".

7.43 In *European Communities – Computer Equipment*²⁸, as well as other cases²⁹, the Appellate Body has considered whether a lack of specificity in a request for the establishment of a panel has prejudiced the respondent. In that regard, we do not accept Canada's assertion that a lack of

²⁶ *European Communities – Customs Classification of Certain Computer Equipment*, Report of the Appellate Body, WT/DS62/AB/R-WT/DS67/AB/R-WT/DS68/AB/R, adopted 22 June 1998, paras. 68-70 (footnotes deleted, emphasis added).

²⁷ WT/DS222/1. (We also note that the title of Brazil's request for establishment, which reads *Canada – Export Credits and Loan Guarantees for Regional Aircraft*, albeit assigned by the WTO Secretariat, was accepted by Brazil.)

²⁸ *European Communities – Computer Equipment*, Report of the Appellate Body, footnote 26, *supra*, paras. 58-73.

²⁹ See *Thailand – Anti-dumping Duties on Angles, Shapes, and Sections of Iron or Non-Alloy Steel and H-Beams from Poland*, Report of the Appellate Body, WT/DS122/AB/R, adopted 5 April 2001, paras. 80-97, and *Korea – Dairy*, Report of the Appellate Body, footnote 25, *supra*, paras. 114-131.

specificity in Brazil's request for establishment prevented Canada from preparing and presenting a full defence in this proceeding. We note, in this regard, Brazil's statement that, as indicated in its request for establishment, its claims against the EDC Canada Account (and the EDC Corporate Account and IQ) are limited to the examples cited therein. Brazil submits that it "has neither asserted any right to expand, nor has it in fact expanded, its claims beyond the specific forms of EDC, Canada Account, and IQ export credits listed in its request for establishment"³⁰. Similarly, Brazil's actual claims have been limited to the regional aircraft industry. Thus, given the scope of the claims that Brazil ultimately made in this proceeding, we do not consider that there has been prejudice to the rights of defence of Canada.

7.44 We therefore reject Canada's objection to Claim 1.

(ii) *Claim 2*

7.45 We recall that Claim 2 states:

Canada has not implemented the report of the Article 21.5 panel, adopted by the DSB, requesting that Canada withdraw Canada Account subsidies.

7.46 Canada's request for a preliminary ruling in respect of Claim 2 is based on the lack of reference to a treaty provision in the request for the establishment of a panel as it relates to the requirements set out in Article 6.2 ("a brief summary of the legal basis of the complaint sufficient to present the problem clearly").

7.47 In this regard, we recall that the Appellate Body stated in *Korea – Dairy* that "[i]dentification of the treaty provisions claimed to have been violated by the respondent is *always necessary* both for purposes of defining the terms of reference of a panel and for informing the respondent and the third parties of the claims made by the complainant; such identification is a *minimum prerequisite* if the legal basis of the complaint is to be presented at all"³¹. Further, as noted by the *European Communities – Bed Linen* panel, "[f]ailure to even mention in the request for establishment the treaty Article alleged to have been violated . . . constitutes failure to state a claim at all"³².

7.48 We further note that Article 7.1 of the DSU – which sets out the standard terms of reference for panels – refers to examination of the matter referred to the DSB "in the light of *the relevant provisions* in (name of the covered agreement(s) . . .)".

7.49 We note that Claim 2 contains no reference at all to a WTO provision and it is therefore clear that even the "minimum prerequisite" of Article 6.2 is not fulfilled. Brazil has not supplied the elements necessary for Claim 2 to fall within our terms of reference. Accordingly, we find that Brazil's Claim 2 does not fall within our terms of reference.

(iii) *Claim 5*

7.50 We recall that Claim 5 states:

³⁰ Response of Brazil to Oral Statement of Canada Regarding Jurisdictional Issues at the First Meeting of the Panel, para. 12 (Annex A-8).

³¹ *Korea – Dairy*, footnote 25, *supra*, para. 124 (emphasis added).

³² *European Communities – Anti-Dumping Measures on Imports of Cotton-Type Bed Linen from India* ("*European Communities – Bed Linen*"), Report of the Panel, WT/DS141/R, adopted 12 March 2001, para. 6.15.

Export credits, including financing, loan guarantees, or interest rate support by or through the EDC are prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.

7.51 Canada's request for a preliminary ruling in respect of Claim 5 is based on the breadth of the terms "export credits" and "EDC" in the request for the establishment of a panel as it relates to the requirements set out in Article 6.2.

7.52 In respect of this preliminary objection, we consider that our analysis of the objection to Claim 1 (*See* paragraphs 7.37-7.44, *supra*) applies here as well. We therefore reject Canada's objection to Claim 5.

(iv) *Claim 7*

7.53 We recall that Claim 7 states:

Export credits and guarantees provided by *Investissement Québec*, including loan guarantees, equity guarantees, residual value guarantees, and "first loss deficiency guarantees" are prohibited export subsidies within the meaning of Articles 1 and 3 of the Agreement.

7.54 Canada's request for a preliminary ruling in respect of Claim 7 is based on the breadth of the terms "export credits" and "*Investissement Québec*" in the request for the establishment of a panel as it relates to the requirements set out in Article 6.2.

7.55 In respect of this preliminary objection, we consider that our analysis of the objection to Claim 1 (*See* paragraphs 7.37-7.44, *supra*) applies here as well. We therefore reject Canada's objection to Claim 7.

C. PROGRAMMES "AS SUCH"

1. **Mandatory/discretionary distinction**

7.56 We recall that Brazil claims that the EDC Canada and Corporate Accounts and *IQ* are "as such" prohibited export subsidies contrary to Article 3.1(a) of the SCM Agreement. Given that Brazil's claims are in respect of the programmes as such, the mandatory/discretionary distinction would traditionally apply. Under that distinction – employed in both GATT and WTO cases over the years³³ – only legislation that requires a violation of GATT/WTO rules could be found to be inconsistent with those rules.

³³ *See United States – Anti-Dumping Act of 1916*, Report of the Panel, WT/DS136/R-WT/DS162/R, and Report of the Appellate Body, WT/DS136/AB/R-WT/DS162/AB/R, adopted 26 September 2000, *United States – Measures Affecting the Importation, Internal Sale, and Use of Tobacco*, Report of the Panel, BISD 41S/131, adopted 4 October 1994, *Thailand – Restrictions on Importation of and Internal Taxes on Cigarettes*, Report of the Panel, BISD 37S/200, adopted 7 November 1990, *European Economic Community – Regulation on Imports of Parts and Components*, Report of the Panel, BISD 37S/132, adopted 16 May 1990, *United States – Taxes on Petroleum and Certain Imported Substances (Superfund)*, Report of the Panel, BISD 34S/136, adopted 17 June 1987.

We also note the statement of the Appellate Body in *United States – Hot-Rolled Steel* that "[t]he captive production provision does not, by itself, *require* an exclusive focus on the merchant market, nor does it *compel* a selective approach to the analysis of the merchant market that *excludes* an equivalent examination of the captive market. The provision also does not itself *mandate* that particular weight be accorded to data pertaining to the merchant market. Rather, as explained above, the provision allows the USITC to examine the

7.57 In this regard, we recall that the panel in *United States – Export Restraints* stated:

There is a considerable body of dispute settlement practice under both GATT and WTO standing for the principle that only legislation that *mandates* a violation of GATT/WTO obligations can be found as such to be inconsistent with those obligations. This principle was recently noted and applied by the Appellate Body in *United States – Anti-Dumping Act of 1916* ("1916 Act"):

[T]he concept of mandatory as distinguished from discretionary legislation was developed by a number of GATT panels as a threshold consideration in determining when legislation as such – rather than a specific application of that legislation – was inconsistent with a Contracting Party's *GATT 1947* obligations.

. . .

[P]anels developed the concept that mandatory and discretionary legislation should be distinguished from each other, reasoning that only legislation that mandates a violation of GATT obligations can be found as such to be inconsistent with those obligations.³⁴

7.58 We note that Brazil expressly "agrees . . . that the distinction between discretionary ('as applied') and mandatory ('as such') legislation is an established principle of GATT and WTO jurisprudence"³⁵. There is, therefore, no disagreement between the parties regarding the applicability of the mandatory/discretionary distinction.³⁶

7.59 Accordingly, we shall apply the mandatory/discretionary distinction in this dispute in determining whether the Canadian programmes at issue are as such inconsistent with WTO obligations, i. e., whether the legal texts governing the establishment and operation of these programmes are mandatory in respect of the violations alleged by Brazil. In other words, to assess

merchant market *and* the captive market, with the same degree of care and attention, as part of a broader examination of the domestic industry as a whole . . . Accordingly, if and to the extent that it is interpreted in a manner consistent with our reasoning, as set forth in paragraphs 203 to 208 of this Report, we see no necessary inconsistency between the captive production provision, *on its face*, and the *Anti-Dumping Agreement*" (*United States – Anti-Dumping Measures on Certain Hot-Rolled Steel Products from Japan* ("*United States – Hot-Rolled Steel*"), Report of the Appellate Body, WT/DS184/AB/R, adopted 23 August 2001, para. 208) (footnote omitted, emphasis in original).

³⁴ *United States – Measures Treating Export Restraints as Subsidies* ("*United States – Export Restraints*"), Report of the Panel, WT/DS194/R, adopted 23 August 2001, para. 8.4 (footnotes omitted).

³⁵ Response of Brazil to Question 28 from the Panel, Responses of Brazil to Questions from the Panel Following the First Meeting of the Panel (Annex A-9). We further note that the panels in *Canada – Aircraft* as well as *Brazil – Aircraft* applied the mandatory/discretionary distinction as did the Appellate Body in those cases (*Canada – Aircraft*, Reports of the Panel and the Appellate Body, footnote 9, *supra*, and *Brazil – Export Financing Programme for Aircraft* ("*Brazil – Aircraft*"), Reports of the Panel and the Appellate Body, WT/DS46/R and WT/DS46/AB/R respectively, adopted 20 August 1999). Finally, we note that Brazil argued that the mandatory/discretionary distinction should be applied in *Brazil – Aircraft – Second Article 21.5* (*Brazil – Export Financing Programme for Aircraft – Second Recourse by Canada to Article 21.5 of the DSU* ("*Brazil – Aircraft – Second Article 21.5*"), Report of the Panel, WT/DS46/RW/2, adopted 23 August 2001).

³⁶ We note that the *Section 301* Panel found that even discretionary legislation may violate certain WTO obligations (*See United States – Sections 301-310 of the Trade Act of 1974*, Report of the Panel, WT/DS152/R, adopted 27 January 2000, para. 7.53). We recall that the Panel's analysis in that dispute focused on the nature of the obligations imposed by Article 23.2(a) of the DSU. Neither party has suggested that similar considerations apply in respect of the provisions of the SCM Agreement that Brazil alleges were violated in this dispute.

Brazil's claim against the EDC as such, we must determine whether the EDC programme mandates the grant of prohibited export subsidies in a manner inconsistent with Article 3.1(a) of the SCM Agreement.

7.60 Brazil argues, however, that the mandatory/discretionary distinction should be applied in the "substantive context" of the EDC, i. e., the fact that the EDC is an export credit agency, and that the very purpose of ECAs is to subsidise exports. Brazil explains that its reference to "substantive context" is drawn from the following statement by the panel in *United States – Export Restraints*:

We are not aware of any GATT/WTO precedent that would require a panel to consider whether legislation is mandatory or discretionary *before* examining the substance of the provisions at issue. To the contrary, we note that a number of panels, in disputes concerning the consistency of legislation, have *not* considered the mandatory/discretionary question in the abstract and as a necessarily threshold issue. Rather, the panels in those cases first resolved any controversy as to the requirements of the GATT/WTO obligations at issue, and only then considered *in light of those findings* whether the defending party had demonstrated adequately that it had sufficient discretion to conform with those rules. That is, the mandatory/discretionary distinction was applied *in a given substantive context*.³⁷

7.61 We note, however, that the Panel in that case was primarily addressing the issue of whether the mandatory/discretionary distinction had to be addressed by a panel as a threshold matter as argued by the United States in that case, or whether a panel could address this distinction after considering the legal requirements of the applicable provisions of the WTO Agreement. In other words, the phrase "substantive context" refers to Articles 1 and 3 of the SCM Agreement³⁸, and not the measure under review. The point made by the panel in *United States – Export Restraints* is simply that it may be difficult to determine whether non-conforming conduct is mandated, without first determining what the obligations are against which conformity is measured. In the present case, the relevant "substantive context" in applying the mandatory/discretionary distinction would be the obligations set forth in Article 3.1(a) of the SCM Agreement, and not the programmes under review.

7.62 We shall therefore apply the mandatory/discretionary distinction in light of Article 3.1(a) of the SCM Agreement. In other words, the question we must address is whether the EDC – the EDC Canada Account and the EDC Corporate Account – or *IQ* requires Canada to provide subsidies contingent upon export performance within the meaning of Article 3.1(a) of the SCM Agreement.

7.63 We recall that Article 3 of the SCM Agreement states, in relevant part:

Except as provided in the Agreement on Agriculture, the following subsidies, within the meaning of Article 1, shall be prohibited:

(a) subsidies contingent, in law or in fact, whether solely or as one of several other conditions, upon export performance, including those illustrated in Annex I; (footnotes deleted)

³⁷ *United States – Export Restraints*, footnote 34, *supra*, para. 8.11 (emphasis in original, footnote omitted).

³⁸ The Panel in *United States – Export Restraints* stated: "[I]dentifying and addressing the relevant WTO obligations first will facilitate our assessment of the manner in which the legislation addresses those obligations, and whether any violation is involved. That is, it is after we have considered both the substance of the claims in respect of WTO provisions and the relevant provisions of the legislation at issue that we will be in the best position to determine whether the legislation requires a treatment of export restraints that violates those provisions" (*United States – Export Restraints*, footnote 34, *supra*, para. 8.12).

7.64 We further recall that Article 1 of the SCM Agreement states:

1.1 For the purpose of this Agreement, a subsidy shall be deemed to exist if:

(a)(1) there is a financial contribution by a government or any public body within the territory of a Member (referred to in this Agreement as "government"), i.e. where:

(i) a government practice involves a direct transfer of funds (e.g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e.g. loan guarantees);

(ii) government revenue that is otherwise due is foregone or not collected (e.g. fiscal incentives such as tax credits [footnote omitted]);

(iii) a government provides goods or services other than general infrastructure, or purchases goods;

(iv) a government makes payments to a funding mechanism, or entrusts or directs a private body to carry out one or more of the type of functions illustrated in (i) to (iii) above which would normally be vested in the government and the practice, in no real sense, differs from practices normally followed by governments;

or

(a)(2) there is any form of income or price support in the sense of Article XVI of GATT 1994;

and

(b) a benefit is thereby conferred.

Thus, Article 1.1 makes clear that the definition of a subsidy has two distinct elements (i) a financial contribution (or income or price support), (ii) which confers a benefit.

7.65 Thus, in this case, Brazil would have to demonstrate that the legal instruments governing the establishment and operation of the programmes at issue are mandatory in respect of the alleged violation, i. e., the grant of prohibited export subsidies. In other words, Brazil would have to demonstrate that the legal instruments mandate (i) a financial contribution; (ii) which confers a benefit, and a subsidy therefore exists, and (iii) that subsidy is contingent upon export performance.

7.66 We note that Canada has not contested that the legal instruments governing the programmes at issue mandate financial contributions. We also note that Article 1.1(a)(1)(i) indicates that a financial contribution exists where "a government practice involves a direct transfer of funds (e. g. grants, loans, and equity infusion), potential direct transfers of funds or liabilities (e. g. loan guarantees)". We consider that there is no disagreement between the parties that the legal instruments governing the programmes at issue mandate such activity.

7.67 We note, however, that the parties do not agree that the legal instruments governing the programmes at issue mandate conferral of a benefit and establish export contingency. We shall address those questions in the context of each programme. With respect to the conferral of a benefit, which we shall address first, we will be guided by the relevant findings of the panel in *Canada – Aircraft*. In that case, the panel found that:

First, in our opinion the ordinary meaning of "benefit" clearly encompasses some form of advantage. We do not consider that the ordinary meaning of "benefit" *per se* includes any notion of net cost to the government. As Canada itself has noted, the dictionary definition of "benefit" refers to "advantage", and not to net cost. In order to determine whether a financial contribution (in the sense of Article 1.1(a)(i)) confers a "benefit", *i.e.*, an advantage, it is necessary to determine whether the financial contribution places the recipient in a more advantageous position than would have been the case but for the financial contribution. In our view, the only logical basis for determining the position the recipient would have been in absent the financial contribution is the market. Accordingly, a financial contribution will only confer a "benefit", *i.e.*, an advantage, if it is provided on terms that are more advantageous than those that would have been available to the recipient on the market.³⁹

Further, the Appellate Body upheld the findings of the panel, ruling as follows:

We also believe that the word "benefit", as used in Article 1.1(b), implies some kind of comparison. This must be so, for there can be no "benefit" to the recipient unless the "financial contribution" makes the recipient "better off" than it would otherwise have been, absent that contribution. In our view, the marketplace provides an appropriate basis for comparison in determining whether a "benefit" has been "conferred", because the trade-distorting potential of a "financial contribution" can be identified by determining whether the recipient has received a "financial contribution" on terms more favourable than those available to the recipient in the market.⁴⁰

7.68 Thus, we shall now examine whether the legal instruments governing the programmes at issue mandate subsidisation, in particular, the conferral of a benefit within the meaning of Article 1 of the SCM Agreement. If that is the case – and a subsidy therefore exists – we will examine whether that subsidy is contingent upon export performance.

2. Export Development Corporation "as such"

7.69 The EDC is incorporated under the laws of Canada and is wholly owned by the Government of Canada. Canada explains that the EDC operates on commercial principles⁴¹ with the objectives of:

- (a) supporting and developing, directly or indirectly, Canada's export trade; and
- (b) supporting and developing, directly or indirectly, Canada's capacity to:
 - (i) engage in exports, and
 - (ii) respond to international business opportunities.⁴²

7.70 We note that Brazil makes a broad argument in respect of the EDC as such – in terms of the EDC Corporate and Canada Accounts being export credit agencies – which applies to both the EDC Corporate and Canada Accounts. Brazil also makes certain additional arguments which are specific to each of the two accounts. We shall first address the broad argument encompassing both accounts and

³⁹ *Canada – Aircraft*, Report of the Panel, footnote 9, *supra*, para. 9.112 (footnote omitted).

⁴⁰ *Canada – Aircraft*, Report of the Appellate Body, footnote 9, *supra*, para. 157.

⁴¹ First Written Submission of Canada, para. 19 (Annex B-4).

⁴² *Export Development Act*, RSC 1985, c. E-20, s. 10 (Exhibit BRA-17).

then the additional arguments specific to each account, applying the mandatory/discretionary distinction to all three sets of arguments.

(a) Export Development Corporation as an export credit agency

(i) *Brazil*

7.71 Brazil's broad argument regarding the EDC as such is that the EDC Corporate and Canada Accounts "are established and operate as export credit agencies ["ECAs"] that have as the *raison d'être* of their existence the provision of export subsidies"⁴³. Brazil claims that ECAs operate with an unfair competitive advantage, as they are able to raise funds at a lower cost than their private sector competitors, and because they are exempted from certain taxes. Thus, when the EDC provides guarantees, loans, and financial services, it necessarily confers a benefit. The fact that the EDC operates on "commercial principles" does not eliminate this unfair competitive advantage, nor the benefit. Brazil asserts that the safe haven of item (k) of the Illustrative List was created precisely because the provision of prohibited export subsidies is "inherent in the very existence and functioning of an ECA"⁴⁴.

7.72 Brazil further claims that specific examples demonstrate that the EDC as such provides prohibited export subsidies in the form of loan guarantees, financial services, and debt financing.

(ii) *Canada*

7.73 Canada argues that Brazil, by its argument that all ECAs necessarily provide prohibited export subsidies, seeks to escape its burden of proving the existence of a subsidy and, in particular, a benefit. In the opinion of Canada, Brazil's argument is not supported by the text of the SCM Agreement, and it is contrary to what previous panels and the Appellate Body have found to constitute a subsidy. As ECAs vary with respect to legal status, policies, and products, they do not necessarily subsidise exports, according to Canada. Canada considers that the test of whether an ECA offers a subsidy is not "Is it an ECA?", but whether the recipient of the financing receives a financial contribution on terms more favourable than those available to the recipient in the market, as per the finding of the Appellate Body in *Canada – Aircraft*.

7.74 Canada disputes Brazil's attempt to refer to individual transactions to defend its "as such" claim. According to Canada, a Member cannot look to individual transactions to illustrate that a measure is inconsistent as such. To prove that a measure is inconsistent as such, a Member must prove that the executive is legally required to act in a manner inconsistent with the WTO Agreement in some circumstances.

(iii) *Findings*

7.75 We note that, as is well established in WTO dispute settlement, the initial burden of proof lies on the complaining party, which must establish a *prima facie* case of inconsistency. The burden then shifts to the defending party, which must counter or refute the claimed inconsistency. We recall, in this regard, the statement of the Appellate Body in *Hormones*:

The initial burden lies on the complaining party, which must establish a *prima facie* case of inconsistency with a particular provision of the *SPS Agreement* on the part of the defending party, or more precisely, of its SPS measure or measures complained

⁴³ Response of Brazil to Question 29 from the Panel, Responses of Brazil to Questions from the Panel Following the First Meeting of the Panel (Annex A-9).

⁴⁴ See footnote 35, *supra*.

about. When that *prima facie* case is made, the burden of proof moves to the defending party, which must in turn counter or refute the claimed inconsistency.⁴⁵

Thus, in this case, Brazil must demonstrate *prima facie* inconsistency in respect of the EDC.

7.76 We recall that Brazil's broad argument is that the EDC as such provides export subsidies as the EDC Corporate and Canada Accounts "are established and operate as [ECAs] that have as the *raison d'être* of their existence the provision of export subsidies"⁴⁶, which would be a violation of Article 3.1(a) of the SCM Agreement. Whatever the reason for the existence of export credit agencies, to prove that the EDC as such provides export subsidies, Brazil would have to establish that to be the case on the basis of the various legal texts regarding the establishment and operation of the EDC (i. e., both its Canada and its Corporate Accounts).

7.77 We consider that, despite the fact that Brazil has the burden of proof, it has not pointed to any specific provision in those legal texts that suggests that these programmes mandate subsidisation, in particular, the conferral of a benefit within the meaning of Article 1 of the SCM Agreement. We have nonetheless examined the various legal texts submitted by Brazil and found nothing that points to mandatory subsidisation on the part of the EDC. We note, in particular, that Article 10 of the *Export Development Act* ("*EDA*")⁴⁷, which sets out the purposes and powers of the EDC, does not support Brazil's claim of mandatory subsidisation. Article 10(1), which sets out the purposes of the EDC, states:

The [EDC] is established for the purposes of supporting and developing, directly or indirectly, Canada's export trade and Canadian capacity to engage in that trade and to respond to international business opportunities.

7.78 Article 10(1.1) of the *EDA*, which sets out the powers of the EDC, enumerates a number of activities that the EDC may engage in, including:

- (a) acquire and dispose of any interest in any property by any means;
- (b) enter into any arrangement that has the effect of providing, to any person, any insurance, reinsurance, indemnity or guarantee;
- (c) enter into any arrangement that has the effect of extending credit to any person or providing an undertaking to pay money to any person;
- (d) take any security interest in any property;
- (e) prepare, compile, publish and distribute information and provide consulting services;
- (f) procure the incorporation, dissolution or amalgamation of subsidiaries;
- (g) acquire and dispose of any interest in any entity by any means;

⁴⁵ *European Communities – Measures Concerning Meat and Meat Products (Hormones)*, Report of the Appellate Body, WT/DS26/AB/R-WT/DS48/AB/R, adopted 13 February 1998, para. 98. See also *United States – Measure Affecting Imports of Woven Wool Shirts and Blouses from India*, Report of the Appellate Body, WT/DS33/AB/R, adopted 23 May 1997, p. 14.

⁴⁶ See footnote 43, *supra*.

⁴⁷ *Export Development Act*, footnote 42, *supra*, Article 10(1).

(h) make any investment and enter into any transaction necessary or desirable for the financial management of the [EDC];

...

7.79 None of these provisions, nor any other provisions of the EDA, establish mandatory subsidisation in respect of the EDC. Further, Article 19 indicates that the Board of Directors of the EDC may determine the terms and conditions on which the EDC may exercise any power under the EDA, and we have seen no evidence presented by Brazil in respect of any terms and conditions set by the Board that would suggest the mandatory grant of subsidies.

7.80 Brazil submits that ECAs benefit from a competitive advantage over their private sector competitors (because ECAs do not pay taxes, for example), and this enables them to offer more favourable terms than those available in the private sector. According to Brazil, "not paying taxes is illustrative of, and an essential prerequisite to, an ECA's capability to perform its normal mission – to provide export subsidies"⁴⁸. Brazil also implies that there would be no need for the EDC if it did not provide support on terms more favourable than those available on the market.⁴⁹ Whether or not these arguments are factually correct, however, we do not see how they establish mandatory subsidisation. That an entity enjoys certain fiscal advantages does not in and of itself prove that that entity is required to pass on those advantages to its clients in the form of subsidies within the meaning of Article 1 of the SCM Agreement.⁵⁰

7.81 In our opinion, the fact that ECAs may have a competitive advantage that allows them to undercut private sector competitors does not mean that they are necessarily required to do so. Furthermore, although the EDC may have provided subsidies in the form of loan guarantees, financial services or debt financing in specific transactions⁵¹, it does not follow from this that the EDC is required to provide such subsidies.

7.82 We note that Brazil submits that "[i]f an ECA is not covered by the safe haven of item (k), it is providing a prohibited subsidy 'as such' because providing export subsidies, as the Tokyo Round negotiators realised, is inherent in the very existence and functioning of an ECA"⁵². . . "[I]tem (k) allows ECAs to perform their normal function and, at the same time, meet GATT, and now WTO, requirements"⁵³. By this, we understand Brazil to be arguing that there would have been no need for item (k) if ECAs did not provide export subsidies. Again, Brazil's argument is predicated on the nature of ECAs, which we do not consider dispositive of the question of mandatory subsidisation. We consider that item (k) sets out the circumstances in which the grant of export credits, *inter alia*, is *per se* deemed to be an export subsidy, and provides one specific exception thereto, otherwise known as the "safe haven" of item (k). The existence of item (k) – including its negotiating history – has no bearing on the question of whether an ECA is mandated to provide subsidies. To accept that because item (k) was negotiated in order to reconcile OECD and WTO rules on export subsidies, it follows that all ECAs are required to grant export subsidies would be to make an assumption for which we see no basis and effectively fail to apply the mandatory/discretionary distinction. The existence of

⁴⁸ Second Written Submission of Brazil, para. 47 (Annex A-10).

⁴⁹ See Exhibit BRA-54.

⁵⁰ Further, to the extent that Brazil might be implying that all ECAs grant prohibited export subsidies, we consider that such an argument blurs the distinction between financial contribution and benefit. That an ECA provides export credits demonstrates the existence of a financial contribution, not the conferral of a benefit thereby.

⁵¹ We are making no findings, however, in this respect at this juncture.

⁵² Second Written Submission of Brazil, para. 45 (Annex A-10).

⁵³ Response of Brazil to Question 28 from the Panel, Responses of Brazil to Questions from the Panel Following the First Meeting of the Panel (Annex A-9).

item (k) does not eliminate the requirement for a complaining party to prove the mandatory nature of the programme in order to prevail on an "as such" claim.

7.83 Finally, we recall Brazil's further argument that specific examples demonstrate that the EDC as such provides prohibited export subsidies in the form of loan guarantees, financial services, and debt financing. "As such" claims are, however, subject to the mandatory/discretionary distinction and, under that distinction, alleged subsidisation would have to be demonstrated on the basis of the various legal texts regarding the establishment and operation of the EDC. In our view, specific instances of subsidisation therefore do not in and of themselves establish "as such" illegality in respect of an underlying programme.

7.84 Having found that the EDC does not – by virtue of being an ECA – mandate the conferral of a benefit and, hence, subsidisation, we need not, and do not, address the question of export contingency.

7.85 For the foregoing reasons, we reject Brazil's argument that the EDC – by virtue of being an ECA – mandates subsidisation, in particular, the conferral of a benefit within the meaning of Article 1 of the SCM Agreement. We therefore find that the EDC is not – by virtue of being an ECA – inconsistent with Article 3.1(a) of the SCM Agreement.

(b) EDC Canada Account

7.86 Having examined Brazil's broad argument encompassing both accounts, we shall now turn to Brazil's additional arguments specific to each account, first addressing Brazil's additional arguments specific to the EDC Canada Account, and then its additional arguments specific to the EDC Corporate Account. Accordingly, to assess Brazil's claim against the EDC Canada Account as such, we must first determine whether the EDC Canada Account mandates the grant of prohibited export subsidies in a manner inconsistent with Article 3.1(a) of the SCM Agreement.⁵⁴

7.87 We recall that the EDC may undertake and administer financing transactions that it would not otherwise undertake provided that the Government of Canada deems them to be in the national interest. Obligations under such activities are funded by the Government of Canada, and the risk is assumed directly by the Government of Canada. This is the so-called "Canada Account".

(i) *Brazil*

7.88 Brazil claims that Canada has not disputed that EDC support is *de jure* contingent on export, and therefore focuses on the question of subsidisation.

7.89 Brazil submits that the EDC only uses the EDC Canada Account when the terms of its support would not be consistent with "what the relevant borrower has recently paid in the market for *similar terms* and with *similar security*"⁵⁵, and thus could not be provided through the EDC Corporate Account. According to Brazil, the EDC Canada Account support is, therefore, apparently not consistent with what Canada deems to be the market, and thus confers a benefit and constitutes a subsidy. Brazil further asserts that the very existence of the EDC *Canada Account Policy Guideline*⁵⁶ demonstrates that EDC Canada Account support as such constitutes a prohibited export subsidy. Brazil indicates that Canada submitted in the *Canada – Aircraft – Article 21.5* case that, under this guideline, "future Canada Account transactions will be consistent with Canada's obligations under the

⁵⁴ We note that, pursuant to item (k) of the Illustrative List of Export Subsidies annexed to the SCM Agreement, "an export credit practice which is in conformity with [the interest rate] provisions [of the *OECD Arrangement*] shall not be considered an export subsidy prohibited by this Agreement".

⁵⁵ First Written Submission of Canada, para. 67 (emphasis in original) (Annex B-4).

⁵⁶ Exhibit CAN-17 and Appendix A to Exhibit CAN-16.

SCM Agreement in that they will qualify for the safe haven in the second paragraph of item (k)⁵⁷. Brazil points out that the Article 21.5 Panel determined that the Policy Guideline was not sufficient to qualify EDC Canada Account support for the safe haven and, by Canada's own admission, without the protection of the safe haven, EDC Canada Account support constitutes a prohibited export subsidy. For Brazil, "it is the *failure* of the policy guideline . . . that speaks to the nature of EDC's Canada Account 'as such'"⁵⁸.

(ii) *Canada*

7.90 Canada maintains that the EDC Canada Account is discretionary, indicating that the *Canada – Aircraft* Panel found that the programme is discretionary and that there is no reason for the present panel to diverge from this finding. According to Canada, Brazil has not submitted arguments or evidence showing that the *Canada – Aircraft* Panel erred in its findings. Nor, submits Canada, has Brazil offered any basis on which the circumstances giving rise to the *Canada – Aircraft* findings can be distinguished from the circumstances in this dispute.

(iii) *Findings*

7.91 Again, we note that, as is well established in WTO dispute settlement, the initial burden of proof lies on the complaining party, which must establish a prima facie case of inconsistency. The burden then shifts to the defending party, which must counter or refute the claimed inconsistency. Thus, in this case, Brazil must demonstrate prima facie inconsistency in respect of the EDC Canada Account.

7.92 We recall that the panel in *Canada – Aircraft* rejected Brazil's claim that Canada Account debt financing for the export of Canadian regional aircraft as such constituted an export subsidy inconsistent with Article 3.1(a) of the SCM Agreement.⁵⁹ Leaving aside for the moment the issue of

⁵⁷ *Canada – Measures Affecting the Export of Civilian Aircraft – Recourse by Brazil to Article 21.5 of the DSU* ("Canada – Aircraft – Article 21.5"), Report of the Panel, WT/DS70/RW, adopted 4 August 2000, para. 5.61.

⁵⁸ Response of Brazil to Question 49 from the Panel, Responses of Brazil to Questions from the Panel Prior to the Second Meeting of the Panel (Annex A-11).

⁵⁹ See *Canada – Aircraft*, Report of the Panel, footnote 9, *supra*, para. 10.1. See also Section VII.B.1, *supra*. In this regard, we recall, in particular, the statement of the Appellate Body in *Japan – Alcoholic Beverages II* that:

[a]dopted panel reports are an important part of the GATT *acquis* . . . They create legitimate expectations among WTO Members, and, therefore, should be taken into account where they are relevant to any dispute. (*Japan – Taxes on Alcoholic Beverages* ("*Japan – Alcoholic Beverages II*"), Report of the Appellate Body, WT/DS8/AB/R-WT/DS10/AB/R-WT/DS11/AB/R, adopted 1 November 1996, p. 14.)

Noting this passage, the panel in *India – Patents (EC)* stated:

[P]anels are not *bound* by previous decisions of panels or the Appellate Body even if the subject-matter is the same. In examining dispute WT/DS79 we are not legally bound by the conclusions of the Panel in dispute WT/DS50 as modified by the Appellate Body report. However, in the course of "normal dispute settlement procedures" required under Article 10.4 of the DSU, we will take into account the conclusions and reasoning in the Panel and Appellate Body reports in WT/DS50. Moreover, in our examination, we believe that we should give significant weight to both Article 3.2 of the DSU, which stresses the role of the WTO dispute settlement system in providing security and predictability to the multilateral trading system, and to the need to avoid inconsistent rulings[.]. (*India – Patent Protection for Pharmaceutical and Agricultural Chemical Products* ("*India – Patents (EC)*"), Report of the Panel, WT/DS79/R, adopted 2 September 1998, para. 7.30 (emphasis in original).)

export contingency, we first address that of subsidisation, in particular, whether Canada Account mandates the conferral of a benefit within the meaning of Article 1 of the SCM Agreement.⁶⁰

7.93 We recall that, under the mandatory/discretionary distinction, Brazil must demonstrate subsidisation on the basis of the legal texts governing the establishment and operation of the EDC Canada Account. We note, however, that the *EDA*⁶¹, which establishes the EDC, does not give any indication of mandatory subsidisation, nor does Brazil argue that it, or any of the other legal texts, does. In particular, the guidelines that apply, including those, such as Appendix A to the *Policy Directive GEN 000-004 – Submission of Documents to the Government of Canada*⁶² and the *EDC Canada Account Policy Guideline*⁶³, adopted to implement the recommendations of the DSB pursuant to *Canada – Aircraft*, refer only to the OECD Arrangement. The *EDC Canada Account Policy Guideline* states: "For the purposes of an authorisation under subsection 23(1) of the *Export Development Act* of a financing transaction or class of financing transactions, it is the policy of the Minister for International Trade to consider that any such transaction or class of transactions which does not comply with the OECD Arrangement on Guidelines for Officially Supported Export Credits would not be in the national interest."⁶⁴ None of these guidelines is sufficient to establish mandatory subsidisation with regard to the EDC Canada Account. While it may be true that even when a programme complies with the OECD Arrangement, it may – pursuant to the findings of the panel in *Canada – Aircraft – Article 21.5* – involve the grant of prohibited export subsidies contrary to Article 3.1(a) of the SCM Agreement, that is not necessarily the case. In our view, Brazil has pointed to no legal text which demonstrates mandatory subsidisation.

7.94 Brazil argues that the existence of subsidisation, in particular, the conferral of a benefit, in respect of the EDC Canada Account is effectively established by the indication as to the circumstances in which the EDC Canada Account is used, in that the EDC Canada Account is only used when the grant of a subsidy is involved. Brazil's argument – made on the basis of a Canadian statement – is that the EDC Canada Account is used only when the terms of its support would not be consistent with "what the relevant borrower has recently paid in the market for *similar terms* and with *similar security*"⁶⁵, and that this indicates that a benefit is conferred. We see no legal basis for this assertion, however, nor does Brazil indicate any. Moreover, the material before us regarding operation of the EDC Canada Account would suggest that the assertion is not factually correct. Export Development Corporation: Annual Report 1999-2000 Reference Guide reads, in relevant part:

While EDC strives to find ways to structure transactions under its Corporate Account, there are a number of factors which might lead EDC to refer a transaction to Canada Account. The transaction could: exceed EDC's exposure guidelines for a particular country (that is, the maximum amount of business EDC has decided it can prudently undertake in a specific market); involve markets where, for reasons of exceptional risk, EDC is unwilling to support Canadian export business; or it could involve an

⁶⁰ We note that, in the present dispute, Brazil claims that Canada has not disputed that EDC support is *de jure* contingent on export, and therefore focuses on the question of subsidisation.

⁶¹ See footnote 42, *supra*.

⁶² Exhibit CAN-16.

⁶³ Exhibit CAN-17.

⁶⁴ Subsection 23(1) of the *Export Development Act* states: "Where the [EDC] advises the Minister that it will not, without an authorisation made pursuant to this section, enter into any transaction or class of transactions that it has the power to enter into under paragraphs 10(1.1)(a) to (e) or (i) to (k) and the Minister is of the opinion that it is in the national interest that the [EDC] enter into any such transaction or class of transactions, the Minister, with the concurrence of the Minister of Finance, may authorise the [EDC] to do so" (Exhibit BRA-17).

⁶⁵ First Written Submission of Canada, para. 67 (emphasis in original) (Annex B-4).

amount or a term in excess of that which EDC would normally undertake for a single borrower.⁶⁶

7.95 It is clear to us from the cited language that there are various factors in a given transaction which might lead to the use of the EDC Canada, rather than Corporate, Account, and these factors serve as limitations on EDC Corporate Account involvement in any particular transaction. We do not see, however, how the conditions for use of the EDC Canada Account demonstrate the existence of mandatory subsidisation, in particular that the programme requires the conferral of a benefit when used to provide financing assistance. We consider that Brazil has failed to demonstrate that EDC Canada Account support necessarily involves subsidisation. Although we can see that such support might conceivably take the form of subsidisation, there is nothing to suggest that this must, in law, be the case.

7.96 Having found that the EDC Canada Account does not mandate the conferral of a benefit and, hence, subsidisation, we need not, and do not, address the question of export contingency.

7.97 For the foregoing reasons, we reject Brazil's claim that the EDC Canada Account mandates the provision of export subsidies contrary to Article 3.1(a) of the SCM Agreement. We therefore find that the EDC Canada Account as such is not inconsistent with Article 3.1(a) of the SCM Agreement.

(c) EDC Corporate Account

7.98 We now turn to Brazil's additional arguments specific to the EDC Corporate Account. To assess Brazil's claim against the EDC Corporate Account, we must determine whether the EDC Corporate Account *per se* mandates the grant of prohibited export subsidies in a manner inconsistent with Article 3.1(a) of the SCM Agreement.

7.99 We recall that EDC "Corporate Account" activities are the EDC's activities on its own account.

(i) *Brazil*

7.100 Brazil claims that Canada has not disputed that EDC support is *de jure* contingent on export, and therefore focuses on the question of subsidisation.

7.101 Brazil argues that the EDC Corporate Account was established to support exports by providing financial services that the market does not provide. The EDC Corporate Account "complements" the market. It provides interest rates below the CIRR⁶⁷ and for terms that exceed ten years. Yet the CIRR and the ten-year repayment term are, in the words of the OECD Arrangement, "the most generous repayment terms and conditions that may be supported". The Appellate Body has concluded that terms more generous than those provided by the OECD Arrangement are positive evidence of a material advantage; such terms are, *a fortiori*, positive evidence of a benefit. The EDC Corporate Account, by its own description, provides financial services to Canadian exporters – and only to Canadian exporters – on terms superior to the terms specified in the OECD Arrangement and superior to those the exporters could obtain elsewhere. Provision of these services is contingent in law upon export. They therefore constitute a prohibited export subsidy.

(ii) *Canada*

⁶⁶ Export Development Corporation: Annual Report 1999-2000 Reference Guide, p. 7 (Exhibit BRA-23).

⁶⁷ Commercial Interest Reference Rate within the meaning of Article 15 of the *OECD Arrangement*.

7.102 Canada maintains that the EDC Corporate Account is discretionary, indicating that the *Canada – Aircraft* Panel found that the programme is discretionary and that there is no reason for the present panel to diverge from this finding. According to Canada, Brazil has not submitted arguments or evidence showing that the *Canada – Aircraft* Panel erred in its findings. Nor, submits Canada, has Brazil offered any basis on which the circumstances giving rise to the *Canada – Aircraft* findings can be distinguished from those in this dispute.

7.103 Canada further responds that EDC Corporate Account financing is not offered on terms more favourable than those available in the market. It does not confer a benefit within the meaning of Article 1.1(b) of the SCM Agreement and therefore does not amount to a subsidy. As Brazil has failed to show that EDC Corporate Account financing amounts to a subsidy, the issue of export contingency is moot.

7.104 Canada disputes Brazil's attempt to refer to individual transactions to defend its "as such" claim. According to Canada, a Member cannot look to individual transactions to illustrate that a measure is inconsistent as such. To prove that a measure is inconsistent as such, a Member must prove that the executive is legally required to act in a manner inconsistent with the WTO Agreement in some circumstances.

(iii) *Findings*

7.105 Again, we note that, as is well established in WTO dispute settlement, the initial burden of proof lies on the complaining party, which must establish a prima facie case of inconsistency. The burden then shifts to the defending party, which must counter or refute the claimed inconsistency. Thus, in this case, Brazil must demonstrate *prima facie* inconsistency in respect of the EDC Corporate Account.

7.106 Leaving aside for the moment the issue of export contingency, we first address that of subsidisation, in particular, whether the EDC Corporate Account mandates the conferral of benefit within the meaning of Article 1 of the SCM Agreement.⁶⁸

7.107 We recall that, under the mandatory/discretionary distinction, Brazil must demonstrate subsidisation on the basis of the legal texts governing the establishment and operation of the EDC Corporate Account. To satisfy the "benefit" element of Article 1.1 of the SCM Agreement for purposes of a challenge to the EDC Corporate Account as such, Brazil must show that the programme requires conferral of a benefit, not that it could be used to do so, or even that it is used to do so. We note, however, that Brazil points to no legal text in respect of the EDC Corporate Account as establishing mandatory subsidisation. We note, further, that we have found none. The EDA⁶⁹, in particular, which establishes the EDC, does not give any indication of mandatory subsidisation. We also note various other texts⁷⁰ submitted by Canada in this regard, in particular, the *Credit Risk Policy Manual*⁷¹ and the *Policy for Implementing Market-Based and Official Support Transactions*⁷². Nothing in these texts provides any evidence to support the mandated conferral of a benefit in financing supplied through the EDC Corporate Account.

7.108 Rather, there is arguably evidence to the contrary which, while not conclusive, suggests that the EDC Corporate Account is not to be used to provide prohibited export subsidies. The *EDC Credit*

⁶⁸ We note that Brazil claims that Canada has not disputed that EDC support is *de jure* contingent on export, and therefore focuses on the question of subsidisation.

⁶⁹ See footnote 42, *supra*.

⁷⁰ See Exhibits CAN-18-23, 25, 46-47, and 49.

⁷¹ Exhibit CAN-48.

⁷² Exhibit CAN-50.

Risk Policy Manual states, for instance: "EDC will establish pricing levels that are appropriate for the underlying credit risk and other relevant considerations applicable to EDC (e. g., Canada's obligations pursuant to the WTO Agreement and the OECD Consensus)." ⁷³ And the *Policy for Implementing Market-Based and Official Support Transactions* states, for instance: "This policy is intended . . . to provide greater certainty of conformity of EDC's medium-/long-term transactions with applicable international trade agreements, primarily the WTO SCM Agreement and the OECD Arrangement, as facts supporting conformity must be adequately documented for each transaction in accordance with the transaction classification process specified herein." ⁷⁴

7.109 We recall further that Canada states: "In terms of the pricing process, the EDC's transportation group has a committee that reviews and approves the pricing on all transactions in the civil aircraft sector. In setting this pricing, the EDC compares what the relevant borrower has recently paid in the market for *similar terms* and with *similar security*. The EDC then prices according to that benchmark. In the absence of this benchmark, the EDC compares the relevant borrower to borrowers of comparable credit standing in the civil aviation sector for whom a similar credit history exists; the EDC then prices according to this alternative benchmark." ⁷⁵ The *EDC Credit Risk Policy Manual* states: "EDC's credit commitments will be priced with respect to market practices" ⁷⁶. Again, there is nothing to suggest that EDC Corporate Account support must, in law, confer a benefit, and therefore take the form of subsidisation.

7.110 We also recall that Brazil submits that operating on commercial principles does not exclude subsidisation, since certain EDC services / products are not available on the market. According to Brazil, the provision by the EDC Corporate Account of services not available on the market necessarily means that services are provided on terms more favourable than those available on the market. As an example, Brazil refers to the EDC Corporate Account's "ability" to complement the services of banks and other financial institutions. We recall, however, that our terms of reference limit the scope of our enquiries to the universe of export credits. To the extent that any services provided by the EDC Corporate Account are independent of export credits provided by the EDC Corporate Account, we consider that those services are not measures that fall within our terms of reference. To the extent that any such services are part and parcel of export credits provided by the EDC Corporate Account, those services fall within our terms of reference and are part of our assessment of export credits provided by the EDC Corporate Account. In this regard, we consider that any such services could not constitute a financial contribution independently of the export credits in relation to which they are provided.

7.111 Even assuming that the provision of services not available on the market necessarily confers a benefit, the fact that the EDC Corporate Account has the "ability" to provide such services does not necessarily mean that it is required to do so. As noted above, to satisfy the "benefit" element of Article 1.1 of the SCM Agreement for purposes of a challenge to the EDC Corporate Account as such,

⁷³ See footnote 71, *supra*, p. 16. With regard to the legal status of the EDC Credit Risk Policy Manual, we note Canada's statement as follows: "As a self-governing, autonomous Crown corporation, EDC's operating practices and policies are the responsibility of its Board of Directors. The Credit Risk Policy Manual was approved by the Board of Directors, but it is not legislation and consequently is not binding on EDC in the same way as legislation would be. However, any transaction of EDC which is within the authority delegated to EDC management and which departs from the policies in the Manual is not duly authorised unless the transaction is in accordance with an exception to the relevant policy (as approved by the Board of Directors) or the Board approves the transaction itself" (Response of Canada to Question 63 from the Panel, Responses of Canada to Questions from the Panel Following the Second Meeting of the Panel (Annex B-11)).

⁷⁴ See footnote 72, *supra*.

⁷⁵ First Written Submission of Canada, para. 67 (Annex B-4).

⁷⁶ See footnote 73, *supra*.

Brazil would have to show that the programme requires conferral of a benefit, not that it could be used to do so, or even that it is used to do so.⁷⁷

7.112 Having found that the EDC Corporate Account does not mandate the conferral of a benefit and, hence, subsidisation, we need not, and do not, address the question of export contingency.

7.113 For the foregoing reasons, we reject Brazil's claim that the EDC Corporate Account mandates the provision of export subsidies contrary to Article 3.1(a) of the SCM Agreement. We therefore find that the EDC Corporate Account as such is not inconsistent with Article 3.1(a) of the SCM Agreement.

3. *Investissement Québec* "as such"

7.114 Having examined Brazil's claim against the EDC as such, we shall now turn to Brazil's claim against *IQ* as such. Accordingly, to assess Brazil's claim against *IQ* as such, we must first determine whether *IQ* mandates the grant of prohibited export subsidies in a manner inconsistent with Article 3.1(a) of the SCM Agreement.

(i) Brazil

7.115 Brazil asserts that *IQ* constitutes a prohibited export subsidy as such. In respect of mandatory subsidisation, Brazil submits that *IQ* is mandated to provide assistance under Section 28 of the *IQ Act*. Brazil argues that a benefit is necessarily conferred when such assistance takes the form of loan guarantees, because firms buying Bombardier aircraft benefit from the superior credit rating of the Government of Québec. *IQ* equity guarantees also confer a benefit, as a governmental guarantee is provided to equity investors. In response to Canada's defence that fees have been charged for such guarantees, Brazil asserts that Canada has failed to demonstrate that the fees charged by *IQ* are commensurate with those charged by commercial guarantors with A+ or A2 credit ratings to firms wishing to enjoy the benefits of those guarantors' A+ or A2 ratings.

7.116 Brazil notes that, furthermore, the latest decree⁷⁸, issued in 2000 to replenish the *IQ* guarantee fund for the Air Wisconsin transaction, eliminates the requirement that fees be charged. Brazil further notes that Canada still argues that fees are in fact charged. In this regard, Canada relies on paragraph B of the *IQ* criteria⁷⁹ which requires that "*IQ* will not make support available for transactions if the remuneration it is to receive is less than that offered in the market". Brazil submits, however, that a closer look at paragraph B demonstrates otherwise; according to paragraph B, if the "competitive nature" of the transactions requires that *IQ* receive less than it would in the market, it will do so.

7.117 In respect of mandatory export contingency, Brazil asserts that *IQ* support is – on the basis of Decrees 572-2000 and 841-2000 – *de jure* contingent on the export of goods outside of Québec. Brazil submits that contingency on export outside Québec should be sufficient to find export contingency within the meaning of Article 3.1(a), or else Members would be able to subvert the

⁷⁷ This is not a case where EDC Corporate Account support necessarily confers a benefit, and where the only discretion available is that of not providing the support at all. We do not express a view as to whether our approach in this case would be equally applicable in such factual circumstances. Rather, this is a case where Canada has discretion to operate the EDC Corporate Account in such a manner that it does not confer a benefit. Further, we note that the facts before us are unlike those before the Appellate Body in *Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items*. In that case, the Appellate Body was reviewing mandatory legislation. (See *Argentina – Measures Affecting Imports of Footwear, Textiles, Apparel and Other Items*, Report of the Appellate Body, WT/DS56/AB/R, adopted 22 April 1998, paras. 49 and 54.)

⁷⁸ Decree 1488-2000 (Exhibit CAN-36).

⁷⁹ Exhibit CAN-51.

SCM Agreement export subsidy disciplines by introducing subsidy programmes that exclude small parts of their home territories.

(ii) *Canada*

7.118 Canada submits that Section 28 of the *IQ Act* provides "the executive authority" with complete discretion regarding the terms and conditions of the assistance it provides. Canada asserts that *IQ* assistance in regional aircraft transactions is authorised more specifically under certain Decrees, which empower *IQ* to grant guarantees or counter-guarantees up to certain amounts of money. *IQ* enjoys complete discretion under these decrees. Furthermore, by virtue of *IQ*'s transaction evaluation criteria⁸⁰, *IQ* must provide support on market terms. *IQ* therefore cannot mandate the provision of subsidies.

7.119 In respect of export contingency, Canada denies that Decree 572-2000, which conditions assistance on export outside of Québec, has anything to do with aircraft sales financing. Nor does it preclude funding for projects within Québec. In any event, Canada submits that contingency on export outside of Québec does not fall within the scope of the Article 3.1(a) prohibition. "Exportation" within the meaning of the SCM Agreement refers to the movement of goods and services between Members, not within them.

(iii) *Findings*

7.120 We note that, as is well established in WTO dispute settlement, the initial burden of proof lies on the complaining party, which must establish a prima facie case of inconsistency. The burden then shifts to the defending party, which must counter or refute the claimed inconsistency. Thus, in this case, Brazil must demonstrate prima facie inconsistency in respect of *IQ*.

7.121 Leaving aside for the moment the issue of export contingency, we first address the issue of subsidisation, in particular, whether *IQ* mandates the conferral of a benefit within the meaning of Article 1 of the SCM Agreement.

7.122 We recall that Brazil's claim is based on provisions of the *IQ Act* and Decrees 572-2000 and 841-2000. Canada asserts, however, that the Decrees "have nothing to do with aircraft sales financing and are not used for aircraft sales financing"⁸¹. In response, Brazil notes that the Decrees relate to support for the sale of goods, and asserts that because regional aircraft are goods, support for the sale of regional aircraft is covered by the Decrees. Canada responds that "Decree 841-2000 could not apply to financing of Bombardier regional aircraft because it applies only to small enterprises. Decree 572-2000 applies, for the most part, to investments in Québec. However, one of the measures in the Decree provides for loan guarantees intended for buyers outside of Québec for the purchase of goods and services . . . Theoretically, this measure could be used to finance the sale of Bombardier regional aircraft. However, due to [a] Québec content limitation and other restrictions, Decree 572-2000 is not well suited to financing regional aircraft sales and has never been used to do so"⁸². Brazil rebuts these arguments by submitting that nothing in Decree 841-2000 suggests that its application is restricted to small enterprises, adding that there are provisions of the Decree suggesting that it is not restricted to small enterprises.

7.123 To the extent that the Decrees could cover support for the sale of regional aircraft, however, the question we must address is whether such support involves mandatory subsidisation, in particular,

⁸⁰ Exhibit CAN-51.

⁸¹ First Written Submission of Canada, para. 93 (Annex B-4).

⁸² Response of Canada to Question 69 from the Panel, Responses of Canada to Questions from the Panel Following the Second Meeting of the Panel (Annex B-11).

the conferral of a benefit within the meaning of Article 1 of the SCM Agreement. Brazil does not indicate anything in the *IQ Act*⁸³ or in Decrees 572-2000⁸⁴ and 841-2000⁸⁵ that demonstrates necessary subsidisation. Nor have we found any such evidence in these or any other legal texts governing the establishment and operation of *IQ*. We note, in this regard, that Section 28 of the *IQ Act*, which establishes *IQ*, states: "The Government may, where a project is of major economic significance for Québec, mandate the agency to grant and administer the assistance determined by the Government to facilitate the realisation of the project. The mandate may authorise the agency to fix the terms and conditions of the assistance." While Brazil is correct in stating that *IQ* is mandated to provide assistance under Section 28 of the *IQ Act*, nothing in the *IQ Act* suggests that such assistance must take the form of subsidisation, and, in particular, confer a benefit under the SCM Agreement. Rather, *IQ* would seem to have the discretion to determine the terms and conditions of such assistance. Even assuming that *IQ* loan and equity guarantees confer a benefit, the fact that *IQ* may do so does not necessarily mean that it is required to do so. To satisfy the "benefit" element of Article 1 of the SCM Agreement for purposes of a challenge to *IQ* as such, Brazil would have to show, as for purposes of a challenge to the EDC, that the programme requires conferral of a benefit, not that it could be used to do so, or even that it is used to do so.

7.124 Similarly, while Decree 572-2000 enables *IQ* to provide financial support for investment or export projects, and Decree 841-2000 enables *IQ* to provide support for market development projects, nothing in these Decrees demonstrates that that support must take the form of subsidisation. To the contrary, it seems to us that both Decrees allow for the provision of support in other forms and reflect a certain discretion on the part of the agency in respect of the manner in which it undertakes investment or export projects or market development projects, respectively.

7.125 Further, when requested by the Panel to "provide any general or sector-specific regulations, guidelines, policies or similar documents . . . concerning the fixing of the terms and conditions of *IQ* support to the regional aircraft industry"⁸⁶, Canada submitted the "*critères d'évaluation des transactions*" (criteria for the evaluation of transactions)⁸⁷ which are used by the *IQ* Credit Committee in making its recommendations in respect of particular transactions⁸⁸. Nor do these "*critères*" provide any evidence of mandatory subsidisation. In this regard, we note Canada's further statement that, "subject to the 'critères d'évaluation', *IQ* has very broad discretion in deciding whether to provide such support, and the terms and conditions on which it does so"⁸⁹. In our view, Brazil has failed to establish the contrary to be the case in that it has not identified a legal instrument from which it can be demonstrated that *IQ* involves the mandatory grant of subsidies.

7.126 Having found that *IQ* does not mandate the conferral of a benefit and, hence, subsidisation, we need not, and do not, address the question of export contingency.

⁸³ Exhibit BRA-18.

⁸⁴ Exhibit BRA-19.

⁸⁵ Exhibit BRA-20.

⁸⁶ Question 17 from the Panel, Responses of Canada to Questions from the Panel Following the First Meeting of the Panel (Annex B-7).

⁸⁷ Exhibit CAN-51.

⁸⁸ While we note Canada's statement that "the 'critères' do not fix terms and conditions", we also note its statement that "[n]o other guidelines etc. exist fixing the terms and conditions of *IQ* support to the regional aircraft industry . . . [T]here is no updated version of the 'critères d'évaluation'. They have remained the same since *IQ* superseded *SDI* in 1998" (Response of Canada to Question 42 from the Panel, Responses of Canada to Questions from the Panel Prior to the Second Meeting of the Panel (Annex B-9)).

⁸⁹ Response of Canada to Question 42 from the Panel, Responses of Canada to Questions from the Panel Prior to the Second Meeting of the Panel (Annex B-9).

7.127 For the foregoing reasons, we reject Brazil's claim that *IQ* mandates the provision of export subsidies contrary to Article 3.1(a) of the SCM Agreement. We therefore find that *IQ* as such is not inconsistent with Article 3.1(a) of the SCM Agreement.

D. EDC / *IQ* "AS APPLIED"

7.128 Brazil requests "that the Panel find the Canada Account, EDC and *IQ* programmes inconsistent with Canada's obligations under the SCM Agreement as applied on the basis of evidence regarding specific transactions".⁹⁰

7.129 Canada asserts that a challenge "as applied" is the same thing as a challenge to "specific transactions".⁹¹

7.130 In our view, there are a number of reasons why it would not be appropriate for us to make separate findings regarding the EDC and *IQ* programmes "as applied". *First*, we do not consider that Brazil's "as applied" claims are independent of its claims regarding "specific transactions". Indeed, Brazil itself acknowledges that "[i]n order for Brazil to prevail on its 'as applied' claims, the Panel must find that the challenged programmes have been *applied in specific transactions* in a manner that is inconsistent with the SCM Agreement".⁹² Since Brazil's "as applied" claims are not independent of its claims against "specific transactions", and since we make findings regarding "specific transactions", we see no practical purpose in making "as applied" findings.

7.131 *Second*, we are unclear as to what the implications of a finding that a programme "as applied" is inconsistent with Article 3.1(a) of the SCM Agreement would be, particularly in the context of implementation. One possibility is that a panel might find that a programme "as applied" is inconsistent with Article 3.1(a) on the basis of findings that all "specific transactions" undertaken thus far under that programme are inconsistent with Article 3.1(a). In such a case, we fail to see what the value added in making a finding regarding the programme "as applied" would be, since the implications for implementation would not extend beyond those "specific transactions". At most, the implication would be that, in the future, the relevant Member should cease to exercise its discretion in a manner inconsistent with Article 3.1(a). This would add nothing to the basic requirement of Article 3.1(a) itself. Another possibility is that a panel might find that a programme "as applied" is inconsistent on the basis of findings that certain – but not all – "specific transactions" under that programme are inconsistent.⁹³ In this case, the implications for implementation would extend beyond the "specific transactions" in respect of which the panel has made findings. We consider, however, that it would be inappropriate for a panel to extend its findings in this manner.⁹⁴

⁹⁰ Response of Brazil to Question 25 from the Panel, Responses of Brazil to Questions from the Panel Following the First Meeting of the Panel (Annex A-9). See footnote 14, *supra*.

⁹¹ See Second Written Submission of Canada, paras. 48-52 (Annex B-8).

⁹² See Response of Brazil to Question 60 from the Panel (emphasis in original), Responses of Brazil to Questions from the Panel Following the Second Meeting of the Panel (Annex A-14).

⁹³ We wish to clarify that we are not addressing the situation where a Member's discretionary legislation has functionally become mandatory as a result of that Member exercising its discretion under that legislation in such a manner that it has become legally bound to continue to exercise its discretion in that manner in the future.

⁹⁴ To the extent that implementation of an "as applied" finding would imply that a Member must ensure against future exercises of discretion in violation of the SCM Agreement, we recall that the Appellate Body expressed some doubts about such a standard when it noted in *Canada – Aircraft – Article 21.5* that "[t]he use in this standard of 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 ... programme. A standard which, if so read, would, however, 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

7.132 *Third*, we recall our earlier remarks regarding the application of the mandatory / discretionary distinction.⁹⁵ Further, we recall the statement of the panel in *United States – Export Restraints* that "the distinction between mandatory and discretionary legislation has a rational objective in ensuring predictability of conditions for trade. It allows parties to challenge measures that will necessarily result in action inconsistent with GATT/WTO obligations, *before* such action is actually taken"⁹⁶. The conclusion by a panel that a programme is discretionary and therefore is not inconsistent with the WTO Agreement and a subsequent conclusion, by the same panel, that the programme "as applied" (i.e., the manner in which the discretion inherent in that programme has been applied) is inconsistent with the WTO Agreement would be of little value. In our view, findings regarding a programme "as applied" would undermine the utility of the mandatory / discretionary distinction.

7.133 For these reasons, we reject Brazil's claims regarding the EDC and IQ programmes "as applied".

E. INFORMATION GATHERING BY THE PANEL

7.134 In a letter dated 21 May 2001, Brazil asked the panel to exercise its discretion under Article 13.1 of the DSU "to request from Canada documents and other information concerning the terms of any support from 1 January 1995 onward committed or granted by the Export Development Corporation ("EDC"), Canada Account, Investissement Québec ("IQ"), or any subsidiary organizations thereof, in connection with the sale of regional aircraft by Bombardier"⁹⁷. This letter was received prior to the deadlines for the parties' first written submissions. On 12 June 2001, we informed the parties that we do "not consider it appropriate to seek any documents or information from either party until it has at least had an opportunity to review both parties' first written submissions".

7.135 Having reviewed the parties' first written submissions, on 20 June 2001 the Panel asked Brazil "to provide full details of the terms and conditions of Embraer's offer of financing to Air Wisconsin", and Canada "to provide full details of the terms and conditions of its Air Wisconsin transaction". Both parties responded to this request on 25 June 2001. Canada failed to provide a copy of the information to Brazil on that date. Instead, Canada "ask[ed] the Panel to require that when this information is provided to Brazil, its disclosure be restricted to officials of the Government of Brazil and private legal counsel retained and paid for by the Government of Brazil who are directly involved in this dispute settlement proceeding". In a letter to Canada dated 26 June 2001, the Panel noted that Canada's letter of 25 June 2001 "was not copied to Brazil, contrary to paragraph 10 of the Panel's Working Procedures". The Panel further "note[d] that, with the limited exception of paragraph 16, its Working Procedures do not provide for any special procedures regarding the treatment of business confidential information. The Panel does not consider it appropriate to introduce such procedures under the present circumstances, i.e., on the basis of an *ex parte* request, and without an opportunity to consult with Brazil". For those reasons, the Panel returned Canada's submission of 25 June 2001. At the first substantive meeting, Canada informed the Panel that it had not intended to make an *ex parte* communication, and that it was not seeking to introduce any special procedures for the treatment of business confidential information. On that basis, its letter of 25 June 2001 was entered in the record.

7.136 During the course of these proceedings, we also addressed a number of additional requests for information and / or documentation to Canada. Since we are not a commission of enquiry, we did not

compliance measure" (*Canada – Aircraft – Article 21.5*, Report of the Appellate Body, footnote 57, *supra*, para. 38) (emphasis in original).

⁹⁵ See paras. 7.56-7.57, *supra*.

⁹⁶ *United States – Export Restraints*, Report of the Panel, footnote 34, *supra*, para. 8.9 (emphasis in original).

⁹⁷ Communication of 21 May 2001 from Brazil to the Panel (Annex A-2).

consider it appropriate to seek additional information and / or documentation on the basis of Brazil's general request of 21 May 2001. We only considered it appropriate to seek additional information / documentation from Canada on the basis of specific information and / or arguments submitted by Brazil.

F. CANADA ACCOUNT SUPPORT FOR THE AIR WISCONSIN TRANSACTION

7.137 On 10 May 2001, the EDC offered Canada Account financing for the acquisition by Air Wisconsin Airlines Corporation ("Air Wisconsin") of [] Bombardier regional jets. The financing will involve [].⁹⁸ [].

7.138 Brazil claims that the Canada Account financing to Air Wisconsin constitutes a prohibited export subsidy, contrary to Article 3.1(a) of the SCM Agreement. Canada asserts that the Canada Account financing to Air Wisconsin falls within the scope of the safe haven provided for in the second paragraph of item (k) of Annex 1 of the SCM Agreement.

7.139 In order to establish that the Canada Account financing to Air Wisconsin constitutes a prohibited export subsidy, Brazil must demonstrate⁹⁹ that the Canada Account financing constitutes a "financial contribution" that confers a "benefit", within the meaning of Article 1.1 of the SCM Agreement. Brazil must also demonstrate that the Canada Account financing is "contingent ... upon export performance", within the meaning of Article 3.1(a) of the SCM Agreement. However, even if Brazil succeeds in establishing that the Canada Account financing to Air Wisconsin is an export subsidy, we will be precluded from finding that it constitutes a prohibited export subsidy if Canada demonstrates¹⁰⁰ that it falls within the second paragraph of item (k) of the Illustrative List of Export Subsidies set forth in Annex 1 of the SCM Agreement.

1. Is the Canada Account financing to Air Wisconsin an export subsidy?

7.140 We shall first consider whether Brazil has established that the Canada Account offer to Air Wisconsin is a "subsidy", i.e., whether it is a "financial contribution" that confers a "benefit". If so, we shall then consider whether Brazil has established that the subsidy is "contingent ... upon export performance".

(a) Financial contribution

7.141 Brazil asserts that the Canada Account financing to Air Wisconsin is a "financial contribution" because "Minister Tobin stated that it would take the form of a 'loan', which constitutes a direct or potential direct transfer of funds, within the meaning of Article 1.1(a)1(i)".¹⁰¹ Canada does not deny that the Canada Account financing to Air Wisconsin constitutes a "financial contribution".

⁹⁸ See attachment to communication of 25 June 2001 from Canada.

⁹⁹ It is now well established that the initial burden lies on the complaining party, which must establish a prima facie case of inconsistency. The burden then shifts to the defending party, which must counter or refute the claimed inconsistency (See *European Communities – Measures Concerning Meat and Meat Products (Hormones)*, Report of the Appellate Body, WT/DS26/AB/R-WT/DS48/AB/R, adopted 13 February 1998, para. 98).

¹⁰⁰ In our view, the second paragraph of item (k) is available as an exception to the prohibition against export subsidies contained in Article 3.1(a) of the SCM Agreement. Accordingly, the second paragraph of item (k) may be invoked by Canada as an affirmative defence to a claim of violation of Article 3.1(a). In this context, we refer to the second paragraph of item (k) as a "safe haven". As is clear from relevant WTO jurisprudence, the burden of establishing an affirmative defence rests with the party raising it (See, for example, *Brazil – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 55).

¹⁰¹ First Written Submission of Brazil, para. 78 (Annex A-3).

7.142 We note that the Canada Account financing to Air Wisconsin will involve [],¹⁰² [] and is therefore a "financial contribution" within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement.¹⁰³

(b) Benefit

7.143 Brazil's claim of "benefit" is based on two statements made by Minister Tobin, Canada's Industry Minister, while announcing the Canada Account financing to Air Wisconsin.¹⁰⁴ Minister Tobin stated that Canada is providing Air Wisconsin with "a better rate than one would normally get on a commercial lending basis".¹⁰⁵ Minister Tobin also stated that Canada was in this instance "using the borrowing strength and the capacity of the government to give a better rate of interest on a loan than could otherwise be secured by Bombardier".¹⁰⁶

7.144 We recall that a "benefit" is conferred when a recipient receives a "financial contribution" on terms more favourable than those available to the recipient in the market.¹⁰⁷ In our view, Minister Tobin's statements indicate that the Canada Account financing to Air Wisconsin, which will take the form of a loan, will confer a "benefit" because it will be on terms more favourable than those available to the recipient in the market. This is confirmed by the fact that, in these proceedings, Canada itself initially considered the terms of the Canada Account financing to Air Wisconsin to be more favourable than those available in the market¹⁰⁸ (and therefore sought to rely on the item (k) safe haven).

7.145 During the course of these proceedings, however, Canada asserted that the Canada Account financing to Air Wisconsin did not confer a "benefit" because it is no more favourable than financing available to Air Wisconsin on the market, in the form of an offer from Embraer. Canada asserts that the Embraer offer is an appropriate market benchmark against which to measure the Canada Account financing, because []. In other words, Canada assumes that because [], it should necessarily be treated as a market offer.

7.146 In these proceedings, Brazil

"[]".¹⁰⁹

7.147 Given the principle of good faith, we accept Brazil's assertion that []. However, that does not mean that Embraer's offer should be treated as a market offer. In this regard, we note *first* that []. Brazil does not deny that these statements were made.

7.148 *Second*, []. In this regard, we note that Embraer has had frequent recourse to PROEX / BNDES support in the past. According to Brazil, approximately [] per cent of Embraer's export sales

¹⁰² See attachment to communication of 25 June 2001 from Canada. [].

¹⁰³ Brazil also argues that such a loan would also constitute the provision of a "service[]" other than general infrastructure", within the meaning of Article 1.1(a)(1)(iii). In light of our finding under Article 1.1(a)(1)(i), we do not consider it necessary to examine Brazil's argument regarding Article 1.1(a)(1)(iii).

¹⁰⁴ See First Written Submission of Brazil, para. 79 (Annex A-3).

¹⁰⁵ See Transcript of Press Conference of Industry Minister Tobin, 10 January 2001, para. 66 (Exhibit BRA-21).

¹⁰⁶ *Id.*, para. 20.

¹⁰⁷ See *Canada – Aircraft*, Report of the Appellate Body, footnote 9, *supra*, para. 157.

¹⁰⁸ See Response of Canada to Question 10 from the Panel, Responses of Canada to Questions from the Panel Following the First Meeting of the Panel (Annex B-7).

¹⁰⁹ See Response of Brazil to Question 32 from the Panel, Responses of Brazil to Questions from the Panel Following the First Meeting of the Panel (Annex A-9).

of regional jets have involved either BNDES or PROEX support.¹¹⁰ (Canada claims the percentage is much higher).¹¹¹ Similarly, Embraer has reported that "[t]he Brazilian government has been an *important source* of export financing for our customers through the BNDES-*exim* program, administered by BNDES. In addition, Banco do Brasil S.A., which is owned by the Brazilian government, administers the ProEx program, which enables some of our customers to receive the benefit of interest discounts."¹¹² For the reasons in these two paragraphs, we consider that the Embraer offer was made with the expectation of support from the Brazilian Government.

7.149 Furthermore, we recall that Canada itself initially considered the Embraer offer to be below market,¹¹³ and that it restated this view towards the end of these proceedings on 8 August 2001, when it asserted that "it is simply not credible that third-party institutions would provide financing for a relatively low quality credit such as Air Wisconsin []." ¹¹⁴ We also note Brazil's assertion that the terms of Embraer's offer do not constitute the "market".¹¹⁵ At various stages during these proceedings, therefore, both parties have asserted that the Embraer offer was not a "market" offer. For these reasons, we are unable to find that Embraer made a "market" offer to Air Wisconsin (despite the absence of Brazilian Government official support for that offer).¹¹⁶ We are therefore obliged to reject Canada's argument that the Canada Account financing to Air Wisconsin did not confer a "benefit" because it was no more favourable than Embraer's "market" offer.

7.150 In view of the statements made by Minister Tobin upon the announcement of the Canada Account financing to Air Wisconsin, and our view that Embraer's offer was not a "market" offer, we find that the Canada Account financing to Air Wisconsin confers a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement.

(c) Export contingency

7.151 Brazil asserts that the Canada Account financing to Air Wisconsin is "contingent ... upon export performance" (Article 3.1(a) of the SCM Agreement) because "[t]he Canada Account is used to support export transactions"¹¹⁷, and because Canada Account is one way for the EDC to satisfy its

¹¹⁰ See Response of Brazil to Panel Question 58 from the Panel, Responses of Brazil to Questions from the Panel Following the Second Meeting of the Panel (Annex A-14).

¹¹¹ Canada has expressed "considerable reservations regarding the accuracy of Brazil's response" (See Comments of Canada on Responses of Brazil to Questions from the Panel Following the Second Meeting of the Panel, paras. 15-19 (Annex B-14)). According to Canada, Brazil has understated the proportion of Embraer's export sales of regional jets that have involved either BNDES or PROEX support. We do not consider it necessary to address this difference of views between the parties, as Brazil's statement that approximately [] per cent of Embraer's export sales of regional jets have involved either BNDES or PROEX support is sufficient for us to conclude that Embraer has had frequent recourse to PROEX / BNDES support in the past.

¹¹² Embraer, Securities and Exchange Commission Form 20F-2000, p. 75 (emphasis added) (Exhibit CAN-67).

¹¹³ At para. 46 of its first written submission, Canada referred to "Brazil's below-market financing offer to Air Wisconsin" (Annex B-4). In its notification under the *OECD Arrangement*, Canada stated that "[t]he interest rate [offered by Embraer] is substantially lower than the market rate at which a regional airline like Air Wisconsin could borrow" (See Exhibit CAN-52, Section 9).

¹¹⁴ See Response of Canada to Question 67 from the Panel, Responses of Canada to Questions from the Panel Following the Second Meeting of the Panel (Annex B-11).

¹¹⁵ See Second Written Submission of Brazil, paras. 105-106 (Annex A-10).

¹¹⁶ Accordingly, it is not necessary for us to consider whether or not the Canada Account offer to Air Wisconsin was less favourable than Embraer's offer, as alleged by Canada.

¹¹⁷ Brazil cites language from the EDC's website, "How We Work" (Exhibit BRA-16).

"mandate to support and develop Canada's export trade and Canadian capacity to engage in that trade and to respond to international business opportunities"¹¹⁸.

7.152 In addressing Brazil's claim of export contingency, we note *first* that Canada does not deny that the Canada Account financing to Air Wisconsin is "contingent ... upon export performance". *Second*, we note that Canada itself has stated that the mandate of the Canada Account is "to support and develop Canada's export trade and Canadian capacity to engage in that trade and to respond to international business opportunities"¹¹⁹. *Third*, we recall that the EDC, which operates the Canada Account programme, was "established for the purposes of supporting and developing, directly or indirectly, Canada's export trade and Canadian capacity to engage in that trade and to respond to international business opportunities".¹²⁰ We therefore consider that any financing provided by the EDC under the Canada Account is necessarily "contingent ... upon export performance", since anything the EDC does is statutorily for the purpose of "supporting and developing ... Canada's export trade"¹²¹. *Fourth*, we note that the *Canada – Aircraft* panel found that the Canada Account debt financing at issue in that case was "contingent ... upon export performance".¹²² For these reasons, we find that support provided under the Canada Account programme, including the financing to Air Wisconsin, is "contingent in law ... upon export performance" within the meaning of Article 3.1(a) of the SCM Agreement.

(d) Conclusion

7.153 In light of the above considerations, we conclude that the Canada Account financing to Air Wisconsin is an export subsidy. As such, the Canada Account financing will constitute a prohibited export subsidy unless it falls within the scope of the item (k) safe haven.

2. Does the Canada Account financing to Air Wisconsin fall within the item (k) safe haven?

(a) Arguments of the parties

7.154 Canada submits that the Canada Account support to Air Wisconsin falls within the safe haven provided for in the second paragraph of item (k), because it is "in conformity with" the "interest rates provisions" of the *OECD Arrangement*.

7.155 According to Canada, it learned in late October 2000 that Brazil was prepared to finance the sale of Embraer regional jets to Air Wisconsin "on below-market terms".¹²³ The information indicated that Brazil was offering []. Canada considered that it had no choice but to offer Air Wisconsin debt financing on a matching basis. Therefore, Canada offered []. As a pre-condition to the financing, Canada required Air Wisconsin to confirm in writing that Canada's offer was valued by Air Wisconsin as no more favourable, viewed in its entirety, than that offered by Brazil. Air Wisconsin provided such written confirmation on 20 March 2001.

7.156 Canada asserts that the Air Wisconsin transaction is consistent with Canada's SCM Agreement obligations because Canada is merely matching Brazil's offer in a manner consistent with the "interest rates provisions" of the *OECD Arrangement*. Canada's financing on a matching basis thus falls within the exception of the second paragraph of Item (k) in Annex I to the SCM Agreement. In Canada's view, matching in the context of the *OECD Arrangement* qualifies for

¹¹⁸ Brazil refers to an Industry Canada News Release, dated 10 January 2001, concerning, *inter alia*, the sale of Bombardier aircraft to Air Wisconsin (Exhibit BRA-3).

¹¹⁹ Industry Canada News Release, 10 January 2001 (Exhibit BRA-3).

¹²⁰ *Export Development Act*, footnote 42, *supra*, Section 10(1).

¹²¹ *Id.*

¹²² See *Canada – Aircraft*, Report of the Panel, footnote 9, *supra*, para. 9.230.

¹²³ First Written Submission of Canada, para. 43 (Annex B-4).

the "safe haven" because the matching provisions of the *OECD Arrangement*, i.e., Article 29 of the main text and Articles 25 and 31 of Annex III, are in "conformity" with the "interest rates provisions" and indeed are themselves "interest rates provisions." A body of disciplines on matching has been developed in the *OECD Arrangement* in order to "govern" this practice. In particular, Articles 50 through 53 of the main text set out matching procedures. The mere existence of this body of disciplines demonstrates that matching is a legitimate exercise that is permitted by, and conforms to, the *OECD Arrangement*.

7.157 According to Brazil, recourse to the matching provisions of the *OECD Arrangement* does not constitute "conformity with" the "interest rate provisions" of the *OECD Arrangement*. The ordinary meaning of item (k), in its context, along with the object and purpose of the SCM Agreement, supports this interpretation. Furthermore, in Brazil's view Canada failed to respect the provisions of Article 53 of the *OECD Arrangement*, which imposes certain procedural requirements on Participants seeking to match.¹²⁴ Thus, even if matching a derogation could benefit from the item (k) safe haven in principle, Brazil considers that Canada's failure to respect the Article 53 procedural requirements would exclude the item (k) safe haven in this case.

(b) Evaluation by the Panel

7.158 As noted above¹²⁵, the onus is on Canada to establish that the Canada Account financing to Air Wisconsin falls within the scope of the safe haven provided for in the second paragraph of item (k).

7.159 The second paragraph of item (k) provides

... 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 a successor undertaking which has been adopted by those original Members), 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.

7.160 Neither party disputes that the Embraer offer to Air Wisconsin is not consistent with the *OECD Arrangement* [].¹²⁶ To the extent that the Canada Account financing to Air Wisconsin matches the Embraer offer, the Canada Account financing therefore matches a derogation.

7.161 In order to avail itself of the item (k) safe haven, Canada must first establish that the matching of a derogation could, as a matter of law, be "in conformity with" the "interest rates provisions" of the *OECD Arrangement*. Only if Canada establishes that this is possible as a matter of law, will we need to consider whether Canada has met its burden of establishing that the Canada Account financing to Air Wisconsin is matching according to the provisions of the *OECD Arrangement*. Similarly, only if Canada establishes that matching a derogation could, as a matter of law, fall within the item (k) safe

¹²⁴ First, Brazil states that Canada failed to comply with Article 53(a) of the *OECD Arrangement*, whereby Participants "shall make every effort to verify" that terms not conforming with the *OECD Arrangement* are "officially supported". Second, Brazil asserts that Canada has not demonstrated that it informed its fellow Participants of the nature and outcome of the verification efforts called for by Article 53(a). Nor has it provided evidence demonstrating that it notified other *OECD Arrangement* Participants of the terms and conditions of its support for the Air Wisconsin transaction, as it is required to do under Articles 53(b) and 47(a) of the *OECD Arrangement*. Third, Brazil submits that Article 53, which regulates matching of non-conforming terms and conditions offered by a non-participant, does not permit non-identical matching.

¹²⁵ See para. 7.139, *supra*.

¹²⁶ See Articles [] of the *Sector Understanding on Export Credits for Civil Aircraft*.

haven, will we need to address Brazil's arguments regarding Canada's alleged failure to comply with the procedural requirements of Articles 47(a) and 53 of the *OECD Arrangement*.

7.162 In determining whether the matching of a derogation could, as a matter of law, be "in conformity with" the "interest rates provisions" of the *OECD Arrangement*, we recall that Article 31.1 of the *Vienna Convention on the Law of Treaties* provides that a treaty shall be interpreted "in good faith in accordance with the ordinary meaning to be given to the terms of the treaty in their context and in the light of its object and purpose."

7.163 The concept of "conformity" with the "interest rates provisions" of the *OECD Arrangement* was addressed by the panel in *Canada – Aircraft – 21.5*.¹²⁷ That panel considered, on the basis of a textual analysis, that conformity with the interest rates provisions of the *OECD Arrangement* had to be judged on the basis of (i) conformity with the minimum interest rates provision, i.e. the CIRR, and (ii) adherence to those provisions of the *OECD Arrangement* which "operate to support or reinforce the minimum interest rate rule".¹²⁸ The panel considered that its textual analysis was confirmed by the context of the second paragraph of item (k), and the object and purpose of the SCM Agreement.

7.164 With regard to matching, the *Canada – Aircraft – 21.5* panel took the view that offers that matched a permitted exception (an action itself foreseen and permitted within limits by the *Arrangement*) "conformed" with the provisions of the *OECD Arrangement* and, hence, also "conformed" with the interest rates provisions in the sense of the safe haven clause.¹²⁹ In contrast, offers that matched a derogation (an action itself not permitted under any circumstances by the *Arrangement*) were not "in conformity" with the provisions of the *OECD Arrangement* and, as a result, were also not "in conformity" with the interest rates provisions in the sense of the safe haven clause.¹³⁰ The *Canada – Aircraft – Article 21.5* panel stated, in this regard, that, if it were accepted that matched derogations were "in conformity" with the interest rates provisions of the *OECD Arrangement*, then the concept of "conformity" could not possibly discipline official financing support.¹³¹ The *Canada – Aircraft – Article 21.5* panel also recalled that non-Participants to the *OECD Arrangement* would not, as a matter of right, have access to information regarding the terms and conditions offered or matched by Participants. Such information was available only to Participants. Thus, if matched derogations were eligible for the safe haven in the second paragraph of item (k), non-Participants would be at a systematic disadvantage vis-à-vis Participants.¹³² The *Canada – Aircraft – Article 21.5* panel also stressed the importance of avoiding an interpretation of item (k), second paragraph, that would lead to structural inequity in respect of developing country Members.¹³³

7.165 The findings of the *Canada – Aircraft – Article 21.5* panel on item (k) were not appealed by Canada (or Brazil) and were subsequently adopted by the DSB on 4 August 2000. The findings of that panel regarding the exclusion of the matching of a derogation from the item (k) safe haven were found "persuasive" by the *Brazil – Aircraft – Second Article 21.5* panel.¹³⁴ The report of that panel was not appealed by Canada (or Brazil) and was subsequently adopted by the DSB on

¹²⁷ *Canada – Aircraft – Article 21.5*, Report of the Panel, footnote 57, *supra*.

¹²⁸ *Canada – Aircraft – Article 21.5*, Report of the Panel, footnote 57, *supra*, para. 5.114.

¹²⁹ *Id.*, paras. 5.124 and 5.126. The *Canada – Aircraft – Article 21.5* panel referred to Articles 29 and 51 of the *OECD Arrangement* as well as Articles 25, 29(d), and 31 of the *Sector Understanding on Civil Aircraft* (*Id.*, para. 5.124 and footnote 113).

¹³⁰ *Id.*, paras. 5.125-5.126. The *Canada – Aircraft – Article 21.5* panel referred to Articles 29 and 47(b) of the *OECD Arrangement* as well as Articles 25, 29(d), and 31 of the *Sector Understanding on Civil Aircraft* (*Id.*, para. 5.125 and footnote 113).

¹³¹ *Id.*, paras. 5.120 and 5.125.

¹³² *Id.*, para. 5.134.

¹³³ *Id.*, para. 5.136.

¹³⁴ *Brazil – Aircraft – Second Article 21.5*, Report of the Panel, footnote 35, *supra*, para. 5.113.

23 August 2001. We consider that the findings of both the abovementioned panels are persuasive, and endorse those panels' interpretations of the second paragraph of item (k). The approach of these panels appears to us to be entirely consistent with the wording of the second paragraph of item (k). Indeed, if one were to accept that the matching of a derogation could fall within the item (k) safe haven, one would effectively be accepting that a Member could be "in conformity with" the "interest rates provisions" of the *OECD Arrangement* even though that Member failed to respect the CIRR (or a permitted exception). In our view, such an interpretation would be unjustified.

7.166 Canada has sought to distinguish the findings of the *Canada – Aircraft – 21.5* panel.¹³⁵ Canada notes that the panel opined as to which provisions of the *OECD Arrangement* would constitute "interest rates provisions" on the theory that its mandate was to determine what was necessary to "ensure" compliance, and that the panel offered its opinion in the absence of an actual disputed transaction. While Canada's observations may be factually accurate, in our view they do not render the panel's reasoning any less persuasive.

7.167 Canada considers that the matching provisions of the *OECD Arrangement*, i.e., Article 29 of the main text and Articles 25 and 31 of Annex III, are in "conformity" with the "interest rates provisions", and indeed are themselves "interest rates provisions", because a body of disciplines on matching has been developed in the *OECD Arrangement* in order to "govern" this practice. In this regard, Canada refers to the procedures set forth in Articles 50 through 53. We note, however, that Canada argues that the availability of the item (k) safe haven is not conditional on fulfilment of the procedural requirements set forth in Articles 50 – 53 of the *OECD Arrangement*.¹³⁶ In our view, it would be anomalous to find that all forms of matching could in principle fall within the scope of the item (k) safe haven on the basis of the procedures set forth in Articles 50 – 53 of the *OECD Arrangement*, if compliance with those procedures was not required in order to benefit from the item (k) safe haven in a given case.

7.168 Canada also states that the Appellate Body in *Brazil – Aircraft* "mentioned the possibility of using the 'matching' provisions of the *OECD Arrangement*".¹³⁷ We note, however, that the Appellate Body expressly stated that "'matching' in the sense of the *OECD Arrangement* [was] not applicable in [that] case".¹³⁸ The Appellate Body cannot, therefore, be understood to have made any findings on this issue. In addition, we note that there is nothing to suggest that the Appellate Body was referring to the matching of a derogation, as opposed to the matching of a permitted exception. As explained by the *Canada – Aircraft – 21.5* panel, this distinction has significant implications for the application of the item (k) safe haven.¹³⁹

7.169 Canada submits that the text of the *OECD Arrangement* does not support the interpretation of the *Canada – Aircraft – 21.5* panel. In particular, Canada argues that Article 29 specifically permits matching as a response to an "initiating offer" that may or may not comply with the *OECD Arrangement*. According to Canada, it is the initiating offer that may be the derogation, but never the (matching) response, because the initiating offer – when it amounts to a derogation – is

¹³⁵ Although the report of the *Brazil – Aircraft – Second 21.5* panel was not adopted at the time that the parties made their submissions in these proceedings, that panel issued its interim report to the parties on 20 June 2001, before our first substantive meeting with the parties. Thus, although we did not have access to that interim report, the parties could have taken the interim findings of that panel into account for the purpose of making their submissions in the present proceedings.

¹³⁶ Canada submits that the term "interest rates provisions" excludes "procedural requirements with which a non-Participant inherently could not comply", although Canada asserts that matching must nevertheless be "undertaken in good faith and on the basis of reasonable due diligence" (*See* First Written Submission of Canada, para. 56 and footnote 46 (Annex B-4)).

¹³⁷ First Written Submission of Canada, footnote 40 (Annex B-4).

¹³⁸ *Brazil – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 185.

¹³⁹ *See* 7.164, *supra*.

specifically prohibited under Article 27, whereas the (matching) response is specifically permitted by Article 29. We note that Canada made this argument in the *Canada – Aircraft – 21.5* proceedings, and that the panel dealt with Canada's argument by observing that, "although matching of derogations is in certain cases not prohibited, this does not alter the fact that both the original derogation and the matching remain, by the *Arrangement's* own terms *out of conformity* with the provisions of the *Arrangement*."¹⁴⁰ The panel also noted that "Canada's approach would directly undercut real disciplines on official support for export credits".¹⁴¹ We see no reason not to adopt the same approach to Canada's argument in these proceedings. In our view, in such cases the matching interest rate is simply not "in conformity with [the interest rates] provisions", as that expression is used in the SCM Agreement.

7.170 Canada also submits that although the SCM Agreement disciplines trade distorting subsidies, the prospective nature of the dispute settlement remedies means that – in the absence of matching – illegal subsidisers will have a perpetual advantage. According to Canada, incorporating the matching disciplines of the *OECD Arrangement* in the item (k) safe haven prevents this. In our view, however, it is not entirely clear that the WTO dispute settlement system only provides for prospective remedies in cases involving prohibited export subsidies. In this regard, we recall that the *Australia – Leather – Article 21.5* panel found that remedies in cases involving prohibited export subsidies may encompass (retrospective) repayment in certain instances.¹⁴² In any event, even if the WTO dispute settlement mechanism does only provide for prospective remedies, we note that it does so in respect of all cases, and not only those involving prohibited export subsidies. Article 23.1 of the DSU provides that Members shall resolve all disputes through the multilateral dispute system,¹⁴³ to the exclusion of unilateral self-help. Thus, to the extent that the WTO dispute settlement system only provides for prospective remedies, that is clearly the result of a policy choice by the WTO Membership. Given this policy choice, and given the fact that Article 23.1 of the DSU applies to all disputes, including those involving (alleged) prohibited export subsidies, we see no reason why the (allegedly) prospective nature of WTO dispute settlement remedies should impact on our interpretation of the second paragraph of item (k).

7.171 In addition, Canada considers it significant that the Illustrative List of Export Subsidies contained in Annex 1 of the SCM Agreement was carried over from the Tokyo Round Subsidies Code. Canada notes that the *OECD Arrangement* was adopted in 1978, after more than ten years of negotiations. In 1979, the Tokyo Round Subsidies Code was agreed together with other Tokyo Round Agreements. Given that the signatories of the GATT Subsidies Code were at the same time participants in the *OECD Arrangement*, Canada believes it is illogical that the signatories of the GATT Subsidies Code would have allowed matching in the *OECD Arrangement* but then would have forbidden it in the Subsidies Agreement one year later. In our view, it is not our role to pass judgment on the logic of the signatories of the GATT Subsidies Code. Like the *Canada – Aircraft – 21.5* and *Brazil – Aircraft – Second 21.5* panels, we have confined our interpretation to the wording of the second paragraph of item (k), read in context, and in light of the object and purpose of the SCM Agreement. Furthermore, we note that Canada refers to the GATT Subsidies Code in a section of its first written submission concerning the object and purpose of the SCM Agreement. In this regard, we do not consider that the object and purpose of the SCM Agreement is necessarily the same

¹⁴⁰ *Canada – Aircraft – Article 21.5*, Report of the Panel, footnote 57, *supra*, para. 5.125 (emphasis in original).

¹⁴¹ *Id.*

¹⁴² *Australia – Subsidies Provided to Producers and Exporters of Automotive Leather – Recourse by the United States to Article 21.5 of the DSU*, Report of the Panel, WT/DS126/RW, adopted 11 February 2000, para. 6.39.

¹⁴³ Article 23.1 of the DSU states: "When Members seek the redress of a violation of obligations or other nullification or impairment of benefits under the covered agreements or an impediment to the attainment of any objective of the covered agreements, they shall have recourse to, and abide by, the rules and procedures of this Understanding."

as the object and purpose of the GATT Subsidies Code. For example, the SCM Agreement provides for more extensive special and differential treatment for developing countries than the GATT Subsidies Code did. In addition, the preamble to the Marrakesh Agreement Establishing the World Trade Organization, of which Agreement the SCM Agreement is an integral part, recognises "that there is need for positive efforts designed to ensure that developing countries, and especially the least developed among them, secure a share in the growth in international trade commensurate with the needs of their economic development". No such "need" was identified in the GATT Subsidies Code. In addition, all WTO Members are bound by the SCM Agreement, whereas only a number of GATT Contracting Parties were signatories of the GATT Subsidies Code. Furthermore, the provisions of the SCM Agreement – unlike those of the GATT Subsidies Code – are subject to binding dispute settlement under the DSU.

7.172 Canada also notes the statement by the *Canada – Aircraft – 21.5* panel that, with the scope of the item (k) exemption left in the hands of a certain subgroup of WTO Members – the Participants – to define, the second paragraph of item (k) should not be interpreted in a manner that allows that subgroup of Members to create for itself de facto more favourable treatment than under the SCM Agreement than is available to all other WTO Members.¹⁴⁴ Canada asserts that the application of all the "interest rates provisions" of the *OECD Arrangement* – including matching – is not de facto more favourable treatment for Participants, because the right to offer terms on a matching basis is available to all WTO Members. While we accept that all WTO Members would have the right to match derogations, were such matching to fall within the scope of the item (k) safe haven, we note that non-Participants would still be at a "systematic disadvantage as they would not have access to the information about the terms and conditions being offered or matched by Participants".¹⁴⁵ Thus, while both Participants and non-Participants may have the right to match derogations, it cannot be assumed that non-Participants would always have the information needed to exercise that right in practice.¹⁴⁶

7.173 Canada denies that there is any "systematic disadvantage" to non-Participants, as they are under no obligation to provide information on matching offers to anyone. By contrast, Canada notes that Participants must notify their matching, which therefore is subject to prior scrutiny by other Participants. Canada further notes that, although non-Participants would not receive the terms and conditions of Participants' matching offers, Participants would likewise not receive non-Participants' matching offers. Moreover, Canada suggests that non-Participants are advantaged because the *OECD Arrangement* is a public document, and non-Participants therefore know the basic terms and conditions that Participants may offer. However, the terms and conditions of non-Participants' offers are not public knowledge.

7.174 We fail to see how the fact that matching by Participants is subject to prior scrutiny removes the "systematic disadvantage" resulting from the fact that non-Participants will have no formal means of knowing what terms and conditions (offered by Participants) they are entitled to match. Nor is this "systematic disadvantage" for non-Participants removed by the fact that Participants will not receive the terms and conditions of non-Participants' offers. The fact that Participants may not know precisely what terms and conditions are being offered by non-Participants does not change the fact that non-Participants have no formal means of knowing what terms and conditions are being offered by Participants. In addition, we consider that Canada's argument that non-Participants know what

¹⁴⁴ *Canada – Aircraft – Article 21.5*, Report of the Panel, footnote 57, *supra*, para. 5.132.

¹⁴⁵ *Canada – Aircraft – Article 21.5*, Report of the Panel, footnote 57, *supra*, para. 5.134, and *Brazil – Aircraft – Second Article 21.5*, Report of the Panel, footnote 35, *supra*, para. 5.117.

¹⁴⁶ The European Communities argues that if a non-Participant has doubts about the reliability of the alleged offer of non-*OECD Arrangement* terms that it is invited to match, it may request confirmation of them from the offeror. While non-Participants may be able to obtain information in this manner, they would still be at a "systematic disadvantage" compared to Participants in all those situations where Participants notify other Participants, on their own motion, of non-conforming terms, as required by the *OECD Arrangement*.

basic terms and conditions Participants may offer (because the *OECD Arrangement* is a public document) is irrelevant to the issue at hand. We are concerned with the matching of a derogation, which by definition is not in conformity with the terms and conditions of the *OECD Arrangement*. The point is that, while non-Participants may know what terms and conditions Participants are supposed to offer, they have no formal means of knowing when Participants derogate from those terms and conditions.

7.175 The European Communities asserts that the *Canada – Aircraft – 21.5* panel adopted a "strained reasoning" that ignores the informal and "gentleman's agreement" character of the *OECD Arrangement*, a non-binding instrument which is designed to provide a framework for transparency and fair competition in the field of export credit transactions between the participants and to be applied flexibly. According to the European Communities, a more teleological reason for the panel's conclusion was its view that matching would "directly undercut real disciplines on official support for export credits."¹⁴⁷ The European Communities asserts, however, that that view is not shared by the Participants to the *OECD Arrangement* themselves, who obviously regard matching as being compatible with effective disciplines on export credits.¹⁴⁸

7.176 In our view, the fact that the *OECD Arrangement* allows matching of derogations, or the fact that Participants view matching of derogations as a means of disciplining export credits, does not necessarily mean that the SCM Agreement should allow matching of derogations. Unlike the *OECD Arrangement*, the SCM Agreement is not an "informal" "gentleman's agreement". The SCM Agreement therefore does not need to allow recourse to the matching of derogations in order to instil discipline. The SCM Agreement is a binding instrument, and is therefore enforceable through the WTO dispute settlement mechanism.¹⁴⁹

¹⁴⁷ *Canada – Aircraft – 21.5*, Report of the Panel, footnote 57, *supra*, para. 5.125.

¹⁴⁸ A similar argument was expressed by the United States, which referred to the matching provisions of the *OECD Arrangement* as its "key enforcement provision" (Third-Party Submission of the United States, para. 12 (Annex C-2)).

¹⁴⁹ In this regard, we endorse the following findings of the *Brazil – Aircraft – Second 21.5* panel: "It seems to us that both third parties tend to argue – incorrectly – from the standpoint of the *OECD Arrangement* rather than from the standpoint of the safe haven clause and the *SCM Agreement*. The United States considers that it would be unfortunate if Participants to the *OECD Arrangement* were dissuaded from using its matching provisions for fear that doing so might be contrary to the provisions of the *SCM Agreement*. The United States appears to suggest that, deprived of the possibility of matching, Participants would somehow be left defenceless in the face of non-conforming practices under the *OECD Arrangement*. This is not the case, however. It notably overlooks the fact that, to the extent those non-conforming practices are covered by the *SCM Agreement*, they would be enforceable through the WTO dispute settlement mechanism.

The European Communities asserts that the reasoning on matching by the Article 21.5 Panel ignores the fact that the *OECD Arrangement* is a non-binding gentlemen's agreement. The Article 21.5 Panel was well aware of the nature of the *OECD Arrangement*. As we understand it, however, the Article 21.5 Panel based its view on the provisions of the *SCM Agreement* and the need to prevent the scope of the safe haven clause from being improperly enlarged. It convincingly stated that, to accept, for purposes of the *SCM Agreement*, that even non-conforming departures from the provisions of the *OECD Arrangement* were covered by the safe haven, would, in effect, remove any disciplines on official financing support for export credits. The European Communities contests that statement, arguing that the Participants to the *OECD Arrangement* consider matching to be compatible with effective disciplines on officially supported export credits. However, the fact that the *OECD Arrangement* allows matching of derogations does not logically imply that it should also be allowed under the *SCM Agreement*. Indeed, the *OECD Arrangement* and the *SCM Agreement* are very different. The European Communities itself acknowledges that the *OECD Arrangement* is a non-binding gentlemen's agreement. In those circumstances, matching may serve an important deterrent and enforcement function. That rationale for matching does not apply to the *SCM Agreement*. The *SCM Agreement* is a binding instrument, and it is enforceable through the WTO dispute settlement mechanism. The European Communities' argument is

7.177 The United States contends that the *Canada – Aircraft – 21.5* panel's concern (in para. 5.138) that Canada's interpretation would permit Members to "opt out" of their WTO obligations on the basis of the behaviour of non-Members is misplaced, because if matching is shielded by the item (k) safe harbour, then a Member who matches a non-conforming offer is acting in accordance with its WTO obligations. In our opinion, the concern expressed by the *Canada – Aircraft – 21.5* panel was that a "Member's conformity with GATT/WTO rules [should not be] defined by the behaviour of non-Members". We agree. This concern would arise even if the inclusion of the matching of a derogation in the item (k) safe haven would mean that matching Members were acting in accordance with their WTO obligations. This is because the inclusion of the matching of a derogation in the item (k) safe haven would not establish any objective benchmark against which to determine whether or not a Member is in accordance with its WTO obligations. In any given case, the benchmark would be set by reference to the terms and conditions of the non-conforming offer. To the extent that the non-conforming offer were made by a non-WTO Member, the benchmark for determining whether or not a matching Member acts in accordance with its WTO obligations would therefore be the non-conforming terms and conditions offered by the non-Member. Thus, the fact that the matching of a derogation is included in the second paragraph of item (k) would not remove the potential for a "Member's conformity with GATT/WTO rules [to be] defined by the behaviour of non-Members".

7.178 The United States also asserts that, contrary to the *Canada – Aircraft – 21.5* panel's concern, Canada's approach to this issue does not raise the issue of "structural inequity" in respect of developing countries.¹⁵⁰ The United States notes that Article 27 of the SCM Agreement exempts developing countries from the prohibitions of paragraph 1(a) of Article 3, subject to compliance with the provisions in Article 27.4. This exemption applies to all export subsidies, not just to export credits. The United States notes that the exemption in the second paragraph of item (k), by contrast, is much more limited. Despite its more limited scope, however, the United States argues that the item (k) safe harbour was an important part of the overall package that WTO Members agreed to when they accepted the SCM Agreement.

7.179 We understand the United States to argue that the inclusion of the matching of derogations in the item (k) safe harbour would only undermine part of the special and differential treatment provided for developing country members, and that this more limited structural inequity in respect of developing countries should be tolerated because of the importance attached by Members to the item (k) safe harbour. In our view, however, Article 27 accords developing country Members special and differential treatment in respect of all export subsidies, whatever form they take. Thus, to the extent that an export credit constitutes an export subsidy, it falls within the scope of Article 27, and developing country Members are in principle entitled to special and differential treatment in respect of that export credit. We are therefore unable to interpret the second paragraph of item (k) in a manner that would render Article 27, in part at least, ineffective.¹⁵¹

therefore unavailing" (*Brazil – Aircraft – Second 21.5*, Report of the Panel, footnote 35, *supra*, paras 5.114-5.115, footnotes omitted).

¹⁵⁰ We recall that the *Canada – Aircraft – 21.5* panel had referred to the possibility of Canada's interpretation of the second paragraph of item (k) "result[ing] in either more favourable treatment, *de facto*, for developed compared to developing countries, or the *de facto* elimination of special and differential treatment for developing countries" (*Canada – Aircraft – 21.5*, Report of the Panel, footnote 57, *supra*, para. 5.136). That panel referred to the possibility of a developed country Member matching the subsidised terms of a developing country Member, even though those terms are in accordance with a provision according special and differential treatment to that Member, such as Article 27 of the SCM Agreement.

¹⁵¹ See *United States – Standards for Reformulated and Conventional Gasoline*, Report of the Appellate Body, WT/DS2/AB/R-WT/DS4/AB/R, adopted 20 May 1996, p. 23, and *Japan – Alcoholic Beverages II*, Report of the Appellate Body, footnote 59, *supra*, p. 12.

(c) Conclusion

7.180 For the above reasons, we conclude that Canada has failed to establish that the matching of a derogation could, as a matter of law, be "in conformity with" the "interest rates provisions" of the *OECD Arrangement*. As a matter of law, therefore, the matching of a derogation could not fall within the scope of the item (k) safe haven.

7.181 In light of our conclusion in the preceding paragraph, it is not necessary for us to consider whether, as a matter of fact, the Canada Account financing to Air Wisconsin constitutes matching according to the provisions of the *OECD Arrangement*. Similarly, it is not necessary for us to examine Brazil's claims that Canada failed to comply with the procedural requirements set forth in Articles 47(a) and 53 of the *OECD Arrangement*.

3. Conclusion

7.182 We have found that the Canada Account financing to Air Wisconsin is a subsidy that is "contingent ... upon export performance". We have further found that the Canada Account financing, which Canada characterises as the matching of a derogation under the *OECD Arrangement*, cannot as a matter of law benefit from the item (k) safe haven. In light of these findings, we conclude that the Canada Account financing to Air Wisconsin is a prohibited export subsidy, contrary to Article 3.1(a) of the SCM Agreement.

G. OTHER EDC TRANSACTIONS

7.183 Brazil has made detailed claims regarding financing provided by the EDC to the following purchasers of Bombardier regional jets: Atlantic Southeast Airlines ("ASA"), Atlantic Coast Airlines ("ACA"), Comair, Kendell, and Air Nostrum. The EDC provided financing to all of these airlines under the EDC Corporate Account. Some of the EDC financing to Air Nostrum was also provided under the EDC's Canada Account.

7.184 Brazil claims that the abovementioned financing took the form of prohibited export subsidies. Brazil claims that EDC financing is a direct transfer of funds in the form of a loan, which constitutes a "financial contribution" within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement. Brazil also asserts that the provision of loans by the EDC is a "service[] other than general infrastructure", within the meaning of Article 1.1(a)(1)(iii). Brazil claims that EDC financing confers a "benefit" within the meaning of Article 1.1(b), and is therefore a subsidy, because it is provided to the recipient airlines on terms more favourable than the recipients could obtain in the market. Brazil claims that EDC financing is "contingent ... upon export performance" because the EDC was "established ... for the purposes of supporting and developing, directly or indirectly, Canada's export trade and Canadian capacity to engage in that trade and to respond to international business opportunities."¹⁵²

7.185 Canada agrees that EDC financing is a "financial contribution" within the meaning of Article 1.1(a)(1)(i). However, Canada denies that the provision of EDC loans is a "service[] other than general infrastructure", within the meaning of Article 1.1(a)(1)(iii). Canada agrees that the existence of a "benefit" can be determined by examining whether or not a financial contribution is on terms more favourable than those available to the recipient in the market. According to Canada, all Corporate Account financing for regional aircraft since 1998 has been provided on a commercial basis, and therefore does not confer a "benefit". Canada does not deny that EDC support is "contingent ... upon export performance".

¹⁵² *Export Development Act*, footnote 42, *supra*, Section 10(1); Export Development Corporation Annual Report 2000, p. 47 (Exhibit BRA-22).

7.186 In order for Brazil's claims to succeed, it must be demonstrated that the EDC loans at issue are subsidies, by virtue of being "financial contributions" that confer a "benefit". It must also be demonstrated that the EDC financing at issue, if found to constitute subsidisation, is "contingent ... upon export performance".

7.187 We note that the parties agree that the EDC loans at issue take the form of "direct transfer[s] of funds" within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement. We agree, and therefore find that the EDC loans at issue constitute "financial contributions" within the meaning of Article 1.1(a)(1) of the SCM Agreement.¹⁵³

7.188 Brazil makes a number of general arguments in support of its claim that the EDC financing at issue confers a "benefit". These general arguments apply in respect of most of the EDC transactions at issue. Brazil also makes a number of arguments that are transaction-specific, in the sense that they only relate to certain EDC transactions. We begin by examining whether any of the general arguments relied on by Brazil demonstrate that a "benefit" is conferred by the EDC financing at issue. We shall then examine Brazil's transaction-specific arguments. If, on the basis of the above, we find that any of the EDC financing at issue confers a "benefit", we shall then determine whether or not that EDC financing is "contingent ... upon export performance" within the meaning of Article 3.1(a) of the SCM Agreement.

7.189 In addressing Brazil's arguments, we will be guided by the findings of the panel and Appellate Body in *Canada – Aircraft*. In that case, the panel found that

a financial contribution will only confer a "benefit", *i.e.*, an advantage, if it is provided on terms that are more advantageous than those that would have been available to the recipient on the market.¹⁵⁴

7.190 The Appellate Body upheld the findings of the panel, ruling that

the marketplace provides an appropriate basis for comparison in determining whether a "benefit" has been "conferred", because the trade-distorting potential of a "financial contribution" can be identified by determining whether the recipient has received a "financial contribution" on terms more favourable than those available to the recipient in the market.¹⁵⁵

1. Brazil's general "benefit" arguments

7.191 Brazil advances four general arguments in support of its claim that the EDC financing at issue confers a "benefit". First, Brazil asserts that the EDC financing is inconsistent with certain indications of market financing allegedly relied on by Canada in the *Brazil – Aircraft – Second 21.5* proceedings. Second, Brazil asserts that the EDC's financing was offered on the basis of an unreliable credit rating tool. Third, Brazil submits that the EDC financing at issue is more favourable than a "market" benchmark constructed by Brazil on the basis of Enhanced Equipment Trust Certificate ("EETC") data. Fourth, Brazil asserts that the EDC failed to base its terms on financing procured by Bombardier customers from commercial institutions.

¹⁵³ On the basis of this finding, we do not consider it necessary to consider whether or not the provision of EDC financing constitutes the provision of "services other than general infrastructure" within the meaning of Article 1.1(a)(1)(iii) of the SCM Agreement.

¹⁵⁴ *Canada – Aircraft*, Report of the Panel, footnote 9, *supra*, para. 9.112.

¹⁵⁵ *Canada – Aircraft*, Report of the Appellate Body, footnote 9, *supra*, para. 157.

- (a) Indications of market financing allegedly relied on by Canada in the *Brazil – Aircraft – 21.5* proceedings

7.192 Brazil refers to the following statements made by Canada in the *Brazil – Aircraft – 21.5* proceedings:

British Airways, which is the best rated non-Sovereign airline, obtains rates of LIBOR [London Inter-Bank Offer Rate] + 30 to 40 bps for large aircraft deals (an additional 20-30 bps [basis points] should be added for regional aircraft, even for clients with British Airways' credit rating). This translates ... to T [US Treasury fixed rate 10-year notes] + 105-120 (+125-150 for regional aircraft). ... Indeed, AAA-rated industrials (and there are no airlines with this rating) cannot obtain credit at T + 20; AAA's tend to pay a spread of approximately 70 bps.¹⁵⁶

[A] representative sample of airline companies operating in the US market obtained financing at T+110 to 250 basis points (based on a weighted average of the different *tranches* of the financing transaction). It has also noted that the net interest rate payable by a borrower with a particularly poor credit rating may be in excess of T+350 basis points.¹⁵⁷

7.193 According to Brazil, these statements mean that, "in Canada's view, the appropriate spread for the *best-rated* airline for a regional jet transaction would be either LIBOR + 50-70 bps (floating rate) or T-bill plus 125-150 bps (fixed rate transactions). For a '*representative*' airline with a credit rating ranging from AAA to BBB-, the appropriate spread would be up to T-bill + 250 bps. Airlines that are *less credit worthy* have a credit rating 'in excess of T + 350 bps'.¹⁵⁸ Brazil relies on this interpretation of Canada's statements to challenge EDC financing to ASA, ACA, Comair, Kendell, and Air Nostrum.¹⁵⁹

7.194 Canada asserts that Brazil "misrepresents and distorts" Canada's argument in the *Brazil – Aircraft – 21.5* proceedings. According to Canada,

[t]he essence of Canada's argument was that the rate offered under PROEX II [the Brazilian interest rate support programme at issue in *Brazil – Aircraft – 21.5*], US Treasury plus 20 bps, was not available in the market. Moreover, Canada cautioned that although that rate was under no circumstances available, the other rates to which it referred – and to which Brazil now refers in its 31 July statement – do not establish a hard limit for the international aircraft financing market. As Canada explained:

"Prevailing market conditions, different payment profiles, or terms, or other conditions negotiated between a lender and a borrower could affect the final interest rate, resulting in higher or lower rates [than those to which Canada referred in that proceeding]."

Nevertheless, in paragraphs 48 and 49 of its 31 July statement and Exhibit BRA 64, Brazil attempts to attribute to Canada the position that: "For a '*representative*' airline with a credit rating ranging from AAA to BBB-, the appropriate spread would be up

¹⁵⁶ *Brazil – Export Financing Programme for Aircraft – Recourse by Canada to Article 21.5 of the DSU ("Brazil – Aircraft – 21.5")*, Report of the Panel, WT/DS46/RW, adopted 4 August 2000, Annex 1-2, footnote 26.

¹⁵⁷ *Id.*, Annex 1-5, para. 11. We note that a "basis point" is equivalent to 0.01 per cent.

¹⁵⁸ Oral Statement of Brazil at the Second Meeting of the Panel, para. 49 (Annex A-12).

¹⁵⁹ In particular, Brazil claims that the EDC provided financing below the spreads allegedly identified by Canada for "best-rated", "representative" and "less credit worthy" airlines.

to T-bill +250 bps." This is patently false. Exhibit BRA-64 describes the weighted average of particular tranches of airline debt. It does not describe a generically appropriate interest-rate spread based on an airline's credit rating.

Nowhere in the submissions Brazil cites, did Canada argue on the basis of that data that airlines from AAA to BBB- would have to pay spreads of up to 250 bps over US Treasury. Moreover, while Canada pointed out the rates that British Airways was paying at the time as the best-rated non-sovereign airline, Canada did not argue that highly rated airlines would have to pay US Treasury plus 125 bps or more. Canada could not have made such an argument: the data Canada provided (now Brazil's Exhibit BRA-64) shows that American Airlines, which at the time was rated BBB- by Standard & Poor's, was paying, on a weighted average basis, 111 bps over US Treasury.¹⁶⁰

7.195 There is, therefore, significant disagreement between the parties as to how the abovementioned statements by Canada in *Brazil – Aircraft – 21.5* should be interpreted. In our view, Brazil seeks to make more of Canada's statements than is appropriate.¹⁶¹ For example, we do not understand Canada to have advanced generally applicable interest rate spreads based on an airline's credit ratings. In any event, we do not consider it necessary to attempt to resolve the disagreement between the parties concerning Canada's statements in prior proceedings, since we have before us a far more developed factual record than was needed by or available to the panel in *Brazil – Aircraft – 21.5*. Given the volume of data before us, which includes specific spreads levied on airlines with specific credit ratings, we do not consider it necessary to concern ourselves with alleged spreads for general categories of "representative", or "best rated" airlines. To the extent that we have the means to determine what the market would charge for specific airlines with specific credit ratings, we do not consider it necessary to refer to spreads for airlines broadly categorised as "representative", or "best rated".

(b) EDC credit ratings

7.196 Brazil asserts that there are serious questions regarding the reliability of offers based on the output from LA Encore, the EDC's credit rating programme. Brazil raises two issues in this regard. *First*, Brazil asserts that LA Encore is unreliable as an objective tool. *Second*, Brazil asserts that LA Encore overstates credit ratings by four to ten notches.¹⁶² Brazil asserts that, since each notch may account for a difference of approximately 15 basis points in the spread offered to a company,¹⁶³ this discrepancy could make a difference of between 50 and 150 basis points in an offering spread.

LA Encore unreliable as an objective tool

7.197 Brazil considers that LA Encore is unreliable as an objective tool because it has been customised to use subjective factors. Brazil asserts that Canada has not provided any information regarding the precise manner in which the EDC has customised LA Encore, or any description of the subjective factors used in the programme. Brazil asserts that Canada acknowledges that LA Encore underwent a "re-calibration of specific weighting", but does not explain how this was done. Brazil also states that the flexibility and customisation of LA Encore seems to be one of the main

¹⁶⁰ Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel, paras. 22-24 (footnotes omitted, emphasis in original) (Annex B-12).

¹⁶¹ Nevertheless, we note that Canada has not denied in these proceedings that an additional 20-30 basis points should be added to large aircraft spreads in order to arrive at an appropriate spread for regional aircraft transactions.

¹⁶² A firm's credit rating will increase by one "notch" when the new rating is one level higher than the former rating.

¹⁶³ See Oral Statement of Brazil at the Second Meeting of the Panel, para. 54 (Annex A-12).

characteristics of the software. Brazil cites a finding in a report relied on by Canada to the effect that "this flexibility generally precludes the outputs of the system from being used outside the organization. The very attributes that allow extensive customization of the knowledge base for specific credit environments prevent two organizations from being able to objectively use the measure as a basis for transactions since they cannot use the (differently) customised systems as a common basis for comparison."¹⁶⁴

7.198 Canada asserts that LA Encore is a computer-based company analysis software developed by a Certified Public Accounting firm and systems analyst company as a tool for analysing financial risk and comparing, on a broad basis, the financial risks associated with different companies. It is now owned by Moody's Risk Management Services, one of the two largest rating agencies in the world. (As a result, the LA Encore software has been renamed Moody's Risk Advisor, or MRA). LA Encore is used by major commercial banks such as Lloyds, Barclays, and ABN-Amro.

7.199 According to Canada, Moody's maintains each user's system to ensure consistency with the public ratings that it publishes. Moody's permits LA Encore to be tailored using customisation tools to establish or reflect an organisation's own credit practices, policy guidelines or internal ratings approach based on its own lending preferences and portfolio. The EDC has utilised the customisation features of LA Encore to reflect the EDC's own corporate risk methodologies. Canada asserts that this re-calibration of specific weightings has been undertaken to ensure that all EDC-generated ratings take into account a data-base of the current senior unsecured bond ratings of more than 900 S&P rated industrials. This allows the EDC to calibrate its own internally generated ratings with these external market benchmarks. Canada submits that the EDC's risk rating methodologies, which include the re-calibration, have been reviewed in the context of the EDC's credit risk management framework by the external risk management consultants Erisk. According to Canada, Erisk has deemed these methodologies to be in line with standard industry practice.

7.200 We do not understand Brazil to challenge the EDC's use of the LA Encore programme *per se*. Indeed, this would be difficult to accept, given the use of LA Encore by major commercial banks such as Barclays, Lloyd's, and ABN-Amro. Rather, we understand Brazil to challenge the EDC's customisation of its LA Encore programme.

7.201 As noted by Brazil, Moody's has publicised the ability to customise LA Encore (or "Moody's Risk Advisor", as it is now called). According to Moody's, LA Encore incorporates "customisation tools to establish an organisation's own credit practices, policy guidelines or internal ratings approach".¹⁶⁵ Such customisation may take various forms: "authoring" (to adapt the main components of the system to create a unique chart of accounts and reports); "tuner" (to reconfigure subjective questions and adjust their impacts throughout the assessment network); "screen designer" (to adjust the position of questions on the screen); "alerts" (to propagate bank policy with custom messages, help texts and alerts); "reports author" (to build custom report templates); and "administrative tools" (to configure user rights). None of these forms of customisation suggest manipulation for the purpose of providing subsidies. Indeed, we recall that the same programme, with the same scope for customisation, is also used by major commercial banks.

7.202 Canada has explained that the EDC's customisation of LA Encore has comprised the re-calibration of specific weightings, to ensure that all EDC-generated ratings take into account a database of the current senior unsecured bond ratings of more than 900 S&P rated industrials. Although Brazil has complained that Canada has not explained how this re-calibration was performed, Brazil has not argued that there is anything wrong, in principle, with customising in order to take into

¹⁶⁴ R. Kumra *et al.*, "Assessing a Knowledge-based Approach to Commercial Loan Underwriting", Moody's Research Report No. 2-00-1, Revised October 2000, pp. 16-17 (Exhibit CAN-73).

¹⁶⁵ Moody's Risk Advisor (Exhibit CAN-72).

account a data-base of the current senior unsecured bond ratings of more than 900 S&P rated industrials.

7.203 Furthermore, we note that the EDC's customised version of LA Encore is maintained by Moody's, to ensure consistency with the public ratings that it publishes. Accordingly, Moody's would ensure that the EDC's airline ratings would be consistent with Moody's own public airline ratings. We also note Canada's assertion that the EDC's credit rating methodologies, including its customisation of LA Encore, have been verified by Erisk, external risk management consultants, which has deemed these methodologies to be in line with standard industry practice. Brazil has not given us any reason to question Canada's assertion. For these reasons, we are not persuaded by Brazil's arguments regarding the EDC's customisation of LA Encore. In particular, we are not persuaded that Canada's customisation of LA Encore suggests manipulation for the purpose of providing subsidies.

7.204 On the balance of the evidence before us, we reject Brazil's arguments that LA Encore is unreliable as an objective credit rating tool.

Ratings overstated

7.205 Brazil asserts that Canada's methodology to assign credit ratings overstates ratings. Brazil states that "the ratings assigned by Canada to various borrowers were consistently higher than the ratings published for better, more credit worthy airlines".¹⁶⁶ According to Brazil, the "EDC's customised LA Encore system ... produces ratings that are completely at odds with those published by Standard & Poor's".¹⁶⁷

7.206 Brazil has made this argument most particularly in respect of EDC financing provided to Comair. In particular, Brazil notes that "Canada rated Comair at one point as [], even though Standard & Poor's does not give *any* airline this rating and, indeed, Canada itself has stated []".¹⁶⁸ Brazil also notes that the EDC rated Comair [] in March 1998, which – according to the Standard & Poor's data relied on by Brazil – "is a rating no other major US airline has enjoyed".¹⁶⁹

7.207 Canada argues that "[r]atings are not correlated to size. For example, an airline such as Southwest, with total revenues of USD 5.6 billion is rated A by Standard & Pooors and A3 by Moody's. United, a much larger airline with total revenues of USD 19.3 billion has a sub-investment grade rating of BB+/Ba1".¹⁷⁰ According to Canada

[t]hough most regional airlines are not rated, it is false to assume that their ratings would necessarily be lower than the US majors. Indeed, as the following Merrill Lynch commentary notes, in many respects the regional airlines present a lower risk than their major airline counterparts:

Historically, regional airlines have been consistently more profitable than their major counterparts. As such, the stock market has "awarded" them premium valuations vis-à-vis their major partners reflecting their materially better earnings performance and prospects.

¹⁶⁶ Comments of Brazil on Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel, para. 32 (Annex A-17).

¹⁶⁷ Comments of Brazil on Responses of Canada to Questions and Additional Questions from the Panel Following the Second Meeting of the Panel, p. 7 (Annex A-16).

¹⁶⁸ Oral Statement of Brazil at the Second Meeting of the Panel, para. 52 (emphasis in original) (Annex A-12).

¹⁶⁹ *Id.*, para. 90.

¹⁷⁰ Comments of Canada on Responses of Brazil to Questions from the Panel Following the Second Meeting of the Panel, para. 8 (footnote omitted) (Annex B-14).

For example, *SkyWest with only 23 RJs, 90 turboprops and \$530 million of annual revenue has an equity market value of \$1.7 billion – more than Alaska and America West's combined \$1.1 billion!* And those two major airlines generate annual sales, in aggregate of \$3.8 billion, with a combined fleet of 233 large, jet aircraft!

We can only speculate what Comair (and ASA) would be worth at current multiples. *However, we do know that the implied equity value for 100% of ASA and Comair was roughly \$3 billion based on Delta's purchase price a few years ago – which compares to Delta's current equity value of only \$5.8 billion.* [emphasis in original]

Although these comments are meant to reflect equity performance, the underlying facts are relevant to Brazil's assertions. The regional airlines have outperformed the majors in a number of key areas including revenue growth and, in terms of market capitalization, a number of the regional airlines – including Comair and ASA – are the same size if not larger than some of the US majors.

For all of these reasons, Brazil is wrong to suggest that regional airlines should pay more for financing than the major US airlines simply because of their sales revenues.¹⁷¹

7.208 In light of the evidence adduced by Canada, which is based on a report compiled by Merrill Lynch,¹⁷² we are not convinced that Canada's credit ratings for regional airlines are unreliable simply because they are higher than Standard & Poor's public ratings for major US airlines. Canada has explained that regional airlines may be accorded higher credit ratings than major airlines because they have "outperformed the majors in a number of key areas". We note that Comair in particular has been valued very highly by Merrill Lynch. We see no reason why, had Standard & Poor's provided a public rating for Comair,¹⁷³ that public rating would not have reflected the high equity value identified by Merrill Lynch.

7.209 We note Brazil's argument that "Canada rated Comair at one point as [] and, indeed, Canada itself has stated []. Although Brazil does not specify at what point Canada rated Comair as [], we assume that it is referring to Canada's statement that the EDC offered financing to Comair in April 1996 "based on an imputed rating of [], ... Today, given the availability of LA Encore, after inputting Comair's 1994, 1995 and 1996 results into LA Encore we find that the 1996 rating is calculated as []."¹⁷⁴ [] In our view, however, these two statements by Canada are not necessarily inconsistent. Canada did not actually rate Comair as [] in April 1996. Canada simply stated on 26 July 2001, in these proceedings, that it would have rated Comair as [] in April 1996, had it used the LA Encore programme at that time. Further, the fact that Standard & Poor's has not rated major US carriers [] does not necessarily mean that a regional carrier should not be assigned that rating. We therefore draw no conclusions from the fact that [].

¹⁷¹ *Id.*, paras. 10-12 (footnote omitted).

¹⁷² Merrill Lynch, "Regional Airline Update: In Times of Economic Uncertainty, Look to Regional Airlines", 30 May 2001 (Exhibit CAN-103).

¹⁷³ We note that airlines will only request ratings (from companies such as Moody's and Standard & Poor's) when they intend to seek public financing. The fact that regional airlines such as Comair do not have ratings does not reflect on their creditworthiness. It simply means that they have not needed a rating for the purpose of seeking public financing.

¹⁷⁴ Response of Canada to Question 37 from the Panel, Responses of Canada to Questions from the Panel Prior to the Second Meeting of the Panel (Annex B-9).

7.210 Brazil also asserts that there are large changes in ratings assigned to specific regional airlines. Brazil argues that the EDC rated Comair [] in April 1996, but subsequently used its LA Encore programme to generate a rating of [], []. Similarly, the EDC rated ASA as [] in March 1997, but subsequently used its LA Encore programme to generate a rating of [], []. Canada claims that, prior to the introduction of LA Encore, the EDC did not attempt to assign precise credit ratings for potential customers.¹⁷⁵ It simply determined [], []. Brazil did not respond to this Canadian argument when commenting on Canada's 13 August 2001 submission. In addition, there is evidence that the EDC rated ASA [].¹⁷⁶ In light of Canada's assertion regarding the absence of precise credit ratings prior to the introduction of LA Encore, the corroboration of Canada's assertion in respect of ASA, and Brazil's failure to respond to Canada's assertion in its 20 August 2001 submission¹⁷⁷, we attach no importance to the alleged differences between the EDC's pre- and post-LA Encore ratings for Comair and ASA.

7.211 In light of the above, Brazil has not persuaded us that the EDC's credit ratings are overstated.

Conclusion

7.212 To conclude, we find that Brazil has failed to establish that there are serious questions regarding the reliability of offers based on LA Encore output.

(c) Brazil's constructed "market" benchmark

7.213 Brazil asserts that the EDC financing at issue confers a "benefit" because it is more favourable than a "market" benchmark constructed by Brazil using a base EETC¹⁷⁸ spread. Brazil has constructed a "market" benchmark for the majority of the EDC transactions at issue. In establishing its base EETC spread, Brazil first calculated the weighted average of bid spreads at which all airline EETCs were trading in the month of the EDC transaction at issue. Second, as a "cross-check" Brazil calculated the weighted average of offer spreads for all new airline EETCs offered in the year of the EDC transaction at issue.¹⁷⁹

7.214 Canada has criticised the methodology employed by Brazil in respect of EETCs. Without addressing all of the issues raised by Canada,¹⁸⁰ we note that Canada has criticised Brazil's use of data for all EETCs, and Brazil's use of weighted average spreads for all tranches of an EETC.

(i) *Use of data for all EETCs*

7.215 Canada asserts that, although Brazil purported to only include airline EETCs in its base EETC spread,¹⁸¹ it actually included EETC data in respect of non-airlines (i.e., Fed Ex and Atlas Air). According to Canada, only airline EETCs should have been considered. Brazil failed to respond to Canada's objection in its 20 August 2001 submission.

¹⁷⁵ See Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel (Annex B-12).

¹⁷⁶ See 1997 Shadow Bond Rating for ASA (Exhibit CAN-44).

¹⁷⁷ See Comments of Brazil on Responses of Canada to Questions and Additional Questions from the Panel Following the Second Meeting of the Panel (Annex A-16).

¹⁷⁸ Enhanced Equipment Trust Certificates, or EETCs, are a secured form of financing that comprise a number of tranches. Each tranche will be assigned a credit rating, depending on the seniority of the claim of the tranche over the aircraft.

¹⁷⁹ See Comments of Brazil on Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel, paras. 21 and 22 (Annex A-17).

¹⁸⁰ Canada's arguments are set out in full in Annex B-12.

¹⁸¹ See Oral Statement of Brazil at the Second Meeting of the Panel, para. 65 (Annex A-12).

7.216 Given that Brazil itself purported to use only airline EETCs, and in light of Brazil's failure to respond to Canada's objection, we agree with Canada that any EETC data used for the purpose of examining the EDC's financing should not include non-airline EETCs.

(ii) *Use of weighted averages*

7.217 Canada criticises Brazil for using the weighted average spreads for all tranches of an EETC issuance. According to Canada, nowhere has Brazil indicated that it has considered the varying underlying credit ratings of the individual airlines or EETC loan tranches. Neglecting to consider the creditworthiness of different borrowers is a fundamental flaw. Nor does it appear to Canada that Brazil has considered the varying age or type of the underlying assets (for example, whether they are jets at all), or the market's appetite for these assets. According to Canada, Brazil's analysis also fails to address terms to maturity, loan-to-value ratios, liquidity features and cross-collateralisation of the various issues.

7.218 Brazil asserts that Canada stated in *Brazil – Aircraft – Second 21.5* that, for a given EETC, the highest-rated tranche within that EETC was a "conservative relative benchmark" for the purpose of determining "material advantage" within the meaning of the first paragraph of item (k). According to Brazil, "[g]iven that Canada has previously stated that the highest-rated tranche (with the lowest spread) was 'conservative', there is no reason to believe that Brazil's use of weighted-average spreads led in any way to an unfair comparison."¹⁸²

7.219 We recall that EETCs are a secured form of financing that comprise a number of tranches. Each tranche will be assigned a credit rating, depending on the seniority of the claim of the tranche over the aircraft. In our view, the fact that Canada stated that the highest-rated tranche was a "conservative relative benchmark" does not mean that Canada would also consider the inclusion of weighted average spreads for all tranches as an equally "conservative relative benchmark". Indeed, this would only make sense if the use of weighted average spreads for all tranches would necessarily result in a spread that is more "conservative", and therefore lower, than the use of only the highest-rated tranches. However, this will clearly not be the case, since the inclusion of weighted average spreads for all tranches will necessarily include spreads for tranches rated lower than the highest-rated tranche. Thus, the use of weighted average spreads for all tranches of an EETC issuance would result in a benchmark spread that is higher than would be the case if only the spreads for the highest-rated tranches were included. Brazil is therefore wrong to argue that "[g]iven that Canada has previously stated that the highest-rated tranche (with the lowest spread) was 'conservative', there is no reason to believe that Brazil's use of weighted-average spreads led in any way to an unfair comparison."¹⁸³

7.220 Furthermore, it is apparent to us that the use of weighted average spreads for all tranches of an EETC issuance could result in a benchmark spread that is higher than would be the case if only the spreads for the appropriately-rated tranches were included. This could lead to a finding of below-market financing (by reference to Brazil's EETC benchmark), when in fact the transaction at issue may have been at, or above, market. For these reasons, we have considerable reservations regarding Brazil's use of weighted average EETC data, especially given the availability of airline-specific data in the record.

(iii) *Conclusion*

¹⁸² See Comments of Brazil on Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel, para. 15 (Annex A-17).

¹⁸³ In addition, we note that Canada's remarks in *Brazil – Aircraft – 21.5* were made in respect of establishing a market benchmark for the purpose of determining the existence of "material advantage" (item (k), second paragraph). There is no reason for us to assume that Canada would necessarily take the same approach when establishing a market benchmark for the purpose of determining the existence of "benefit".

7.221 In light of the above, we are not persuaded that it is appropriate to rely on Brazil's constructed "market" benchmark for the purpose of determining whether or not the EDC financing at issue confers a "benefit".

(d) Bombardier customers' commercial financing

7.222 Brazil notes that, in its response to Panel Question 43, Canada stated that over [] per cent of Bombardier's sales did not involve any government support, even through so-called "market window" operations.¹⁸⁴ According to Brazil, these transactions would provide a plentiful and accurate resource for determining the appropriate market rates for Canada's officially-supported transactions. Brazil asserts that it is difficult to see how Canada could reasonably arrive at market rates for its transactions without ever referring to the vast majority of Bombardier transactions that it claims were financed without any government participation, even market window participation.

7.223 Canada asserts that where such information is available, the EDC does consider it to the extent that it is relevant. Canada also argues that, to the extent that such information is available, it confirms that the EDC's pricing was at or even above commercial market financing. However, Canada submits that it is often difficult to obtain complete information on the financing provided by banks and other financial institutions due to their confidentiality policies.

7.224 We consider that it would be unrealistic to expect the EDC to have access to data regarding all commercial financing transactions involving Bombardier regional jets. The EDC is not a party to such transactions, and has no right to obtain details of those transactions. Indeed, it is likely that the terms of those transactions are viewed as confidential by the parties.

7.225 In any event, evidence in the record suggests that the EDC has referred to commercial financing for Bombardier regional jets where possible. For example, a December 1996 EDC memo refers to financing from European banks for regional jets purchased by [].¹⁸⁵ In addition, EDC documentation refers to offers of financing by European banks to [].¹⁸⁶

7.226 Thus, we do not consider that EDC financing should be deemed to confer a "benefit" simply because the EDC failed to base its financing in all cases on the terms of commercial financing provided to Bombardier customers.

(e) Conclusion

7.227 In light of the above, we are not persuaded by the general arguments raised by Brazil in support of its claim that the EDC financing at issue confers a "benefit". We shall now examine the transaction-specific "benefit" arguments put forward by Brazil.

2. Brazil's transaction-specific "benefit" arguments

7.228 As noted above, Brazil has made claims concerning specific EDC Corporate Account financing to ASA, ACA, Comair, Kendell, and Air Nostrum. Brazil has also made claims against EDC Canada Account financing to Air Nostrum. We shall now examine each of these transactions in turn, noting that the EDC offered more than one loan to some of these airlines.

¹⁸⁴ The term "market window" is used by the parties to describe the provision of financing by EDC on terms that are, according to Canada, consistent with those that are available in the market.

¹⁸⁵ See Exhibit CAN-59, p. 6.

¹⁸⁶ See Exhibit CAN-39.

Note for public version of report: The Panel accepted Canada's position that the interest rates and fees offered or charged by the EDC and *IQ* should be treated as confidential business information. The Panel noted that detailed knowledge about the considerations and benchmarks it used to determine whether the EDC interest rates at issue conferred a benefit under the SCM Agreement would enable those interest rates to be derived, to varying degrees of precision, for the transactions analysed by the Panel. Accordingly, the Panel concluded that it was necessary to redact significant parts of its report. Nonetheless, the Panel agreed with Brazil that it was important that the considerations and benchmarks used by the Panel be identified. Those considerations and benchmarks included:

- (i) Commercial Interest Reference Rates (CIRRs) (as set by the OECD)
- (ii) the EDC's minimum lending yield (an internal rate set by the EDC)
- (iii) an EETC issued by a major U.S. airline
- (iv) two bond issues of a major U.S. airline
- (v) information on rates reportedly offered by other major banks

The considerations and benchmarks referred to in items (iii) and (iv) were proposed by Canada and were used after consideration of the relevance of their terms and conditions compared to those of the EDC transactions examined. Not all five considerations and benchmarks were used in examining each EDC transaction.

1.229 In examining Brazil's claims in this case, we shall consider whether or not a "benefit" is conferred on Bombardier by virtue of a "benefit" being conferred on the airline customer purchasing Bombardier aircraft.¹⁸⁷ In this regard, Brazil argues that there can be a "benefit" to Bombardier even if there is no "benefit" to the purchasing airline, e.g., even if the EDC provides financing to the purchasing airline on terms that are not more favourable than those that the airline could obtain in the market. In short, Brazil argues that if "Embraer ... offers to arrange financing at γ per cent, while Bombardier is able to provide government financing at γ per cent[,] [t]he government support has benefited Bombardier by relieving it of the necessity of providing or arranging its own financing, even though the customer may view the offers as equal, and therefore not be benefited."¹⁸⁸ In our view, the fact that Bombardier may arrange financing in the form of government support does not necessarily confer a "benefit" simply because Bombardier is "reliev[ed] ... of the necessity of providing or arranging its own financing". If that were the case, a "benefit" would be conferred whenever Bombardier arranged external financing – even through commercial banks – since any external financing would "reliev[e] it of the necessity of providing or arranging its own financing". We find it difficult to accept that the existence of "benefit" (in the context of financing) is determined

¹⁸⁷ We endorse the following statement by the *Brazil – Aircraft – Second 21.5* panel: "We note that PROEX III payments are made in support of export credits extended to the *purchaser*, and not to the *producer*, of Brazilian regional aircraft. In our view, however, to the extent Canada can establish that PROEX III payments allow the purchasers of a product to obtain export credits on terms more favourable than those available to them in the market, this will, at a minimum, represent a *prima facie* case that the payments confer a benefit on the *producers* of that product as well, as it lowers the cost of the product to their purchasers and thus makes their product more attractive relative to competing products" (*Brazil – Aircraft – Second 21.5*, Report of the Panel, footnote 35, *supra*, para. 5.28, footnote 42) (emphasis in original).

¹⁸⁸ See Response of Brazil to Question 59 from the Panel, Responses of Brazil to Questions from the Panel Following the Second Meeting of the Panel (Annex A-14).

on the basis of whether or not Bombardier provides internal or external financing. The existence of "benefit" (in the context of financing) is determined by reference to the terms at which similar financing is available to the airline customer in the market. The abovementioned market comparison indicates that a number of the specific transactions at issue in these proceedings do not confer a "benefit" on the airline customer, and therefore neither on Bombardier. In respect of these specific transactions, Brazil has failed to provide any evidence of "benefit" accruing to Bombardier absent any "benefit" to the airline customer.

(a) ASA – March 1997

7.230 The EDC offered financing to ASA in March 1997. In March 1997, the EDC rated ASA as []. The EDC offered financing at US Ten-Year Treasury Notes (hereinafter "T") plus [] basis points, for [].

7.231 Brazil claims that the terms of the EDC's March 1997 offer to ASA conferred a "benefit" because the repayment term exceeded the maximum authorised under the *OECD Arrangement*, and the spread offered by the EDC was [].¹⁸⁹

(i) *Repayment term*

7.232 Brazil notes that Article 21 of the *Sector Understanding on Export Credits for Civil Aircraft* provides for a maximum repayment term for regional aircraft of 10 years. According to Brazil, a repayment term in excess of 10 years is positive evidence of "material advantage" (within the meaning of item (k), first paragraph) and, a fortiori, a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement.

7.233 Canada claims that the *OECD Arrangement* is not necessarily reflective of market terms. Canada also asserts that repayment terms for regional aircraft financing routinely exceed 10 years.

7.234 In addressing Brazil's argument, we are aware that the Appellate Body found in *Brazil – Aircraft* that "the *OECD Arrangement* can be appropriately viewed as one example of an international undertaking providing a specific market benchmark by which to assess whether payments by governments, coming within the provisions of item (k), are 'used to secure a material advantage in the field of export credit terms'".¹⁹⁰ However, the fact that the *OECD Arrangement* can be used as a market benchmark for the purpose of determining the existence of "material advantage" does not necessarily mean that it should also serve as a benchmark for the purpose of determining the existence of "benefit". If one were to draw this conclusion, one would be equating "benefit" with "material advantage", and the Appellate Body has made it clear that this is not possible as a matter of law. In *Brazil – Aircraft*, the Appellate Body stated that "if the 'material advantage' clause in item (k) is to have any meaning, it must mean something different from 'benefit' in Article 1.1(b)".¹⁹¹

7.235 We note that a "benefit" is only conferred when financing is made available to the recipient on terms more favourable than the recipient could obtain in the market. Thus, Brazil might have been able to demonstrate that a repayment term in excess of ten years confers a "benefit" by establishing that such repayment terms are not available in the market. However, Brazil failed to do this. By contrast, Canada has adduced evidence of instances in which the repayment term of market financing

¹⁸⁹ CIRRs are Commercial Interest Reference Rates within the meaning of Article 15 of the *OECD Arrangement*.

¹⁹⁰ *Brazil – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 181.

¹⁹¹ *Id.*, para. 179 (emphasis in original). The *Brazil – Aircraft – Second 21.5* panel understands the Appellate Body to mean that it is "impermissible" to interpret the term "benefit" to have the same meaning as the term "material advantage" (See *Brazil – Aircraft – Second 21.5*, Report of the Panel, footnote 35, *supra*, footnote 50).

for regional aircraft transactions exceeds 10 years. In particular, Canada has referred the Panel to the 1997 issuance by Northwest Airlines of pass-through certificates financing 12 British Aerospace Avro RJ85 aircraft. The term for the 1997-1A (Class A) certificates is 18.25 years.¹⁹² Canada has also referred the Panel to the 1997 issuance by Continental Airlines of pass-through certificates financing nine Embraer EMB-145ER Regional Jets. The term for the 1997 3A (Class A) certificates is 15.25 years.¹⁹³ In addition, Canada has submitted the Morgan Stanley Dean Witter Report, which offers additional evidence that the standard length of financing available in the market for regional aircraft financing ranges from 10 to 18 years.¹⁹⁴ This report contains information on structured transaction pricing in the commercial marketplace. It indicates that US airlines have financed regional aircraft in the market using enhanced equipment trust certificate (EETC) tranches that feature a greater than 10 year term of maturity. For example, the EETC Class A and B tranches issued on 19 September 1997 by Atlantic Coast Airlines for 6 CRJ-200 and 8 British Aerospace J-41 aircraft have terms of maturity of respectively 16 years (Class A) and 13 years (Class B). In our view, this evidence – which has not been disputed by Brazil – demonstrates that repayment terms of up to 18.25 years are available in the market. Thus, the fact that a given repayment term may exceed the 10-year term provided for in Article 21 of the *Sector Understanding on Export Credits for Civil Aircraft* does not mean *ipso facto* that financing is provided on terms more favourable than those available to the recipient on the market.

7.236 For these reasons, we reject Brazil's argument that a repayment term of more than 10 years is in itself positive evidence of a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement.

(ii) []

7.237 Brazil asserts that the interest rate offered to ASA in March 1997 is []. Brazil argues that an interest rate [] is positive evidence of "material advantage" (item (k), first paragraph) and, a fortiori, a "benefit".

7.238 Canada denies that interest rates [] necessarily confer a "benefit", as the CIRR lags behind the market.

7.239 We have already noted the Appellate Body's finding in *Brazil – Aircraft* that "the *OECD Arrangement* can be appropriately viewed as one example of an international undertaking providing a specific market benchmark by which to assess whether payments by governments, coming within the provisions of item (k), are 'used to secure a material advantage in the field of export credit terms'".¹⁹⁵ We also noted the Appellate Body's statement that "material advantage" should not be equated with "benefit". Furthermore, in *Brazil – Aircraft – 21.5* the Appellate Body stated that "[t]he CIRR is a constructed interest rate for a particular currency, at a particular time, that does not always necessarily reflect the actual state of the credit markets".¹⁹⁶

7.240 Canada has explained that the CIRR lags behind the market, so that at a given point in time financing [] is not necessarily more favourable than that available to the recipient on the market. In this regard, Canada refers the Panel to the following argument it made before the *Brazil – Aircraft – 21.5* panel:

¹⁹² *Northwest Airlines 1997-1 Pass Through Trusts*, Credit Suisse First Boston, Lehman Brothers, Morgan Stanley Dean Witter, Prospectus, 16 September 1997 (Exhibit CAN-54).

¹⁹³ *Continental Airlines 1997-3 Pass Through Trusts*, Morgan Stanley Dean Witter, Prospectus, 23 July 1997 (Exhibit CAN-55).

¹⁹⁴ "EETC Market Update: Monthly Update: Airlines" (Morgan Stanley Dean Witter, Fixed Income Research, North America, Investment Grade Credit – Industrials), 10 February 2001 (Exhibit CAN-14).

¹⁹⁵ *Brazil – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 181.

¹⁹⁶ *Brazil – Aircraft – 21.5*, Report of the Appellate Body, WT/DS46/AB/RW, adopted 4 August 2000, para. 64.

A meaningful comparison of market transactions to CIRR is difficult due to the fact that the CIRR is a constructed rate, while commercial aircraft transactions are priced at commercial rates available at the time of the specific transaction. To recall, the CIRR is determined by taking the average of the 7-year Treasury rate (in the case of deals with repayment terms up to 10 years) for the previous month and adding 100 bps. For example, the CIRR for the period 15 September – 15 October would be constructed using the average of the 7-year Treasury for the month of August, plus 100 bps. Carrying on with the example, the result of this calculation is that the CIRR applicable to transactions closing during the period from 15 September through 15 October would [be] a rate that was calculated using the average of the applicable Treasury rate during August, i.e. up to two months earlier. To an entity that operates on the basis of commercial principles, the calculation of the CIRR is such that it would not be considered a reliable reflection of current market conditions.¹⁹⁷

7.241 Brazil has not disputed that the CIRR lags behind the market.¹⁹⁸ Nor has Brazil disputed that the CIRR may not be a reliable reflection of current market conditions. However, we also note that "CIRRs should represent final commercial lending interest rates in the domestic market of the currency concerned", and "should closely correspond to the rate for first-class domestic borrowers".¹⁹⁹ For this reason, we consider that the CIRR could, in the absence of additional evidence regarding market rates, serve as "a rough proxy for commercial interest rates".²⁰⁰ In our view, therefore, the fact that an interest rate is [] constitutes evidence that the interest rate would be more favourable than rates available in the market, and in the absence of any counter-evidence on market rates, would justify a finding that such an interest rate confers a "benefit".

(iii) *Market benchmarks proposed by Canada*

7.242 Canada has provided evidence that the EDC March 1997 offer to ASA (T plus []) was higher, and therefore less favourable, than the market spreads for a specific tranche of a [], for certain [], and for the general industrial index for similar credit ratings. Canada therefore denies that the EDC March 1997 offer to ASA confers a "benefit".²⁰¹

[]

7.243 Canada compares the EDC's March 1997 offer to ASA with a [].

7.244 Brazil has not expressly challenged Canada's reference to the spreads for specific EETC tranches in these proceedings. On several occasions, Brazil refers to Canada's own references to

¹⁹⁷ *Brazil – Aircraft – 21.5*, Report of the Panel, footnote 156, *supra*, Annex 1-4, Responses of Canada to Questions from the Panel Posed on 3 February 2000, Response to Question 4(a) from the Panel, p. 82.

¹⁹⁸ The "lag" will be more pronounced if market interest rates move quickly, as appears to have happened in the period April 1996 to August 1997 (*See* Exhibit CAN-59).

¹⁹⁹ *OECD Arrangement*, Article 15.

²⁰⁰ *Brazil – Aircraft – Second 21.5*, Report of the Panel, footnote 35, *supra*, para. 5.35 (emphasis in original).

²⁰¹ Brazil notes that Canada has not provided pricing memos for the ASA and ACA transactions. According to Brazil, therefore, the Panel has no way of knowing whether the benchmarks referred to by Canada in Annex II to its 13 August 2001 submission were the actual benchmarks used by EDC to price the transaction, or whether, instead, Canada searched for the specific purpose of this dispute for any benchmark that falls below the rates it offered ASA and ACA. In our view, it is not necessary for a Member to demonstrate that it applied specific benchmarks at the time of providing a "financial contribution" in order to rely on those benchmarks for the purpose of rebutting claims of "benefit". There is no reason why the absence of "benefit" cannot be demonstrated on the basis of an *ex post* rationalisation, provided the benchmarks relied on relate to the time that the transaction was made.

EETC spreads in order to justify Brazil's recourse to EETC data. As noted above, we do not agree with Brazil's use of weighted average EETC data. This does not mean, however, that we should also reject Canada's use of EETC data. This is because Canada does not rely on weighted average EETC data. Rather, Canada has adduced evidence regarding issues of specific EETC tranches. The criteria applied by Canada in selecting these specific EETC tranches (in particular, that the credit rating of the EETC tranche be [], and that the EETC be issued within at least 90 days prior to the Loan's Date of Offer – See Annex II to Canada's submission of 13 August 2001) have not been challenged by Brazil. Since Canada is not relying on average EETC data, and in the absence of any objections raised by Brazil regarding Canada's use of specific EETC tranches, we see no reason not to take into account the specific EETC tranche data submitted by Canada.²⁰²

7.245 We note that the EDC's March 1997 offer to ASA is [] basis points [] than the spread for the [] tranche. Since ASA and the [] tranche were rated [] secured at that time, there is no need to make any credit rating adjustment. However, we note that, according to evidence adduced by Canada, the "vast majority"²⁰³ of EETCs are for large aircraft, and that only one EETC has been placed to finance regional jets.²⁰⁴ From this evidence, we understand that the [] relates to large aircraft. In the *Brazil – Aircraft – Second 21.5* proceedings, Canada asserted that spreads for regional aircraft transactions are 20-30 basis points higher than spreads for large aircraft transactions.²⁰⁵ Accordingly, the EDC's March 1997 offer to ASA should be reduced by 20-30 basis points, to enable a proper comparison with the (large aircraft) [] tranche.²⁰⁶ The adjusted EDC offer would be T + [], which is significantly lower than the spread for the comparable [] tranche identified by Canada.

[]

7.246 Canada has also asserted that the EDC March 1997 offer to ASA was less favourable than [] corporate bonds issued by [], rated [] unsecured, issued in []. In March 1997, the [] were trading at T plus [] and [], i. e., at a lower spread than that offered by the EDC to ASA. These bonds met a number of qualitative criteria set by Canada (in particular, the bonds are [], so they provide a measure

²⁰² In relying on company-specific EETC data, however, we note that both parties have expressed reservations regarding the reliability of EETCs as a market benchmark. For example, Canada asserts that it "never suggested that EETCs could identify the 'market' spread for a particular regional aircraft financing transaction, nor did it rely on EETCs for that purpose" (Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel, para. 31 (Annex B-12)). Brazil asserts that "the credit risk or spread on a EETC issue would generally be lower than the spread that the same airline could obtain in a commercial bank-financed transaction" (Oral Statement of Brazil at the Second Meeting of the Panel, para. 64 (Annex A-12)). We take note of these comments when comparing EDC financing with company-specific EETC data.

²⁰³ Communication of 7 August 2001 from CIT Structured Finance (Exhibit CAN-79).

²⁰⁴ Communication of 8 August 2001 from Babcock & Brown (Exhibit CAN-79).

²⁰⁵ See para. 7.192, *supra*.

²⁰⁶ In its request for interim review (See para. 6.11, *supra*), Canada objected to the Panel's addition of 20-30 basis points to large aircraft EETC spreads to arrive at an appropriate regional aircraft spread. The Panel made this adjustment in response to Brazil's reliance on statements made by Canada in the *Brazil – Aircraft – Second 21.5* proceedings (See paras. 47 and 50 of Oral Statement of Brazil at the Second Meeting of the Panel (Annex A-12)). In responding to Brazil's oral statement (See Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel (Annex B-12)), Canada made no attempt to deny the need for a 20-30 basis point adjustment when converting from large aircraft to regional aircraft spreads. Nor did Canada object to Brazil's inclusion of a 20 basis point adjustment ("for the difference between the regional aircraft used in the financing at issue and the larger jets used in the typical EETC issue") in its Exhibit BRA-66. Furthermore, although Canada asserted at interim review that "[v]ariations in pricing between similar but non-identical asset classes are dynamic and subject to change ...", Canada did not deny the need for an adjustment *per se*. However, although Canada appeared to accept the need for an adjustment of some sort, Canada failed to indicate what would be, in its view, an appropriate adjustment for the transactions at issue. In addition, we note that a lesser adjustment would not necessarily change the outcome of our findings.

of the spread attributed to an airline credit rating, rather than the security provided by an aircraft type, and they have an [] on the date the relevant EDC loan was offered).

7.247 In its 20 August 2001 submission, Brazil accuses Canada of using corporate bonds "in the large aircraft sector without any consideration of whether these spreads should be adjusted for the regional aircraft sector even though ... Canada has said that spreads for the regional aircraft sector should be 20-30 points higher than in the large aircraft sector".²⁰⁷ In this regard, we note that Canada stated in the *Brazil – Aircraft – 21.5* proceedings that "an additional 20-30 bps should be added [to large aircraft spreads] for regional aircraft".²⁰⁸ However, we do not understand Canada to have argued that a regional carrier will necessarily have to pay more for credit than a major carrier. In fact, Canada has expressly argued that this will not necessarily be the case.²⁰⁹ Rather, we understand Canada to have argued that a higher spread will have to be paid for financing purchases of regional aircraft as opposed to large aircraft, since large aircraft offer better security than regional aircraft. Indeed, Brazil itself has argued that this will be the case.²¹⁰ In other words, the spread adjustment depends on the type of aircraft at issue (because regional aircraft offer less security than large aircraft), and not on the nature – or size – of the carrier at issue. As noted above, the two [] relied on by Canada are unsecured, such that they reflect the credit rating of the carrier, and not the security of the aircraft type. Accordingly, Brazil's objection is not a sufficient basis for rejecting Canada's use of the two [] to justify the EDC's March 1997 offer to ASA.

7.248 Brazil has also criticised Canada for using data from one period to justify pricing in another, despite the fact that Canada already criticised Brazil for allegedly doing the same thing (in its oral statement at the second meeting). Thus, Brazil asserts that "Canada relies on the [] issued in March 1997 to support every comparison with the exception of the Atlantic Coast Airlines February 1996 and Kendell Airlines August 1999 offers. Canada uses these bonds as representative comparisons in charts covering financing offered in July 1996 (a year before []), March 1998, August 1998, February 1999, and March 1999".²¹¹ We recall, however, that the relevant []. When these bonds are referred to by Canada, it cites the price at which the bonds were trading at the time of the transaction at issue. Thus, for the ASA March 1997 and August 1998 offers, Canada refers to the March 1997 and August 1998 prices for the relevant []. Similarly, for the EDC's March 1999 offer to ACA, Canada refers to the price at which the [] were trading in March 1999. We therefore reject Brazil's argument that Canada used data from one period to justify pricing in another.

General industrial index

7.249 Canada has also sought to justify the pricing of the EDC's March 1997 offer to ASA on the basis of the spreads for general industrial bonds with similar credit ratings. In particular, Canada has relied on general industrial indices derived from Bloomberg US Fair Market Yields – Industrial.

7.250 Although Brazil has made some limited use of these same general industrial indices,²¹² Brazil believes that the utility of indices of general industrial bonds as a proxy for identifying market rates for financing of regional jet transactions is limited by several factors. First, the 10-year general industrial corporate bonds represent simple averages at which bonds issued by a wide variety of

²⁰⁷ Comments of Brazil on Responses of Canada to Questions and Additional Questions from the Panel Following the Second Meeting of the Panel, para. 27 (footnote omitted) (Annex A-16).

²⁰⁸ *Brazil – Aircraft – 21.5*, Annex 1-2, footnote 26.

²⁰⁹ See paras. 7.207-7.208, *supra*.

²¹⁰ Comments of Canada on Responses of Brazil to Questions from the Panel Following the Second Meeting of the Panel, para. 13 (Annex B-14).

²¹¹ Comments of Brazil on Responses of Canada to Questions and Additional Questions from the Panel Following the Second Meeting of the Panel, para. 26 (Annex A-16).

²¹² See Oral Statement of Brazil at the Second Meeting of the Panel, para. 97 (in respect of ACA) (Annex A-12).

companies in a wide variety of industries are trading at a given point in time. While bonds issued by airlines may be included in the calculation of this average, the average itself does not reveal whether bonds issued by a particular sector should be valued above or below the average at a particular point in time. Second, there are substantial differences in liquidity between the average industrial spreads and a bank loan financing a regional jet purchase. The industrial spreads are based on thousands of bonds being traded in huge volumes (with daily trading volume estimated at \$10 billion) by traders around the world each day. A bank loan to finance a particular purchase of a regional jet, on the other hand, is an isolated transaction, much less liquid, requiring much greater and more immediate assumption of risk by a lender than the lender would experience buying and selling general industrial bonds. Third, general industrial bonds do not accurately reflect the spreads for industry sectors that may not normally be publicly rated or issue corporate bonds, such as many airlines that purchase regional jets. Moreover, the different risks between airline companies and industrial companies are not necessarily reflected in the different ratings of the companies. A major airline rated A-, such as Southwest Airlines, may trade at a different spread than, for example, a major computer company with the same rating. This difference in spreads reflects differences in the market estimation of the prospects for each industry, the nature of the collateral securing each bond, competitiveness within each industry, and the manner in which the bonds are structured within each industry. These factors are reflected to some extent within the ratings, but are largely left to the discretion of the market. According to Brazil, spreads change a lot more frequently than do credit ratings. In the event of a change in the performance of a particular bond issuer or its industry, the market will react much more immediately than will the credit ratings agencies. Brazil submits that the result will be a discrepancy between the spreads at which similarly rated companies in different industries may trade.

7.251 According to Brazil, the market agrees that the general industrials curves do not reflect the peculiarities of the regional airlines industry. For example, in a report on EETCs, Salomon Smith Barney ("SSB") states that "EETCs trade at a considerable premium compared with comparably rated generic corporate bonds."²¹³ SSB's analysis supports Brazil's and the market's views that companies with the same credit rating will not necessarily enjoy the same spreads when issuing papers in the bonds market. Moreover, the similarity in ratings does not in itself mean that companies will obtain financing at the same spreads for particular transactions. For example, Southwest Airlines is a major airline with revenues of \$5.6 billion in 2000 and a fleet of over 350 Boeing large jets and no regional jets.²¹⁴ This is a substantially different company from Atlantic Southeast Airlines (ASA), which had revenues of \$410 million in 1998.²¹⁵ Southwest is currently rated A- by Standard & Poor's.²¹⁶ Assuming that ASA, with less than one-tenth of Southwest's sales revenues,²¹⁷ was also rated A- by the EDC, this does not mean that the market would finance a sale of 20 regional jets to ASA at the same rates as it would finance a sale of the same size to Southwest.

7.252 Canada notes Brazil's argument that the different risks between airline companies and industrial companies are not necessarily reflected in the different ratings of the companies. However, Canada suggests that such individualised risks are taken into account by the EDC in its transaction-specific assessment of risk. Canada also asserts that much of Brazil's criticism of the use of general industrial indices turns on its assertion that smaller companies will not have access to financing at the same rates as larger companies, even when they have the same credit rating. Canada asserts that

²¹³ *The ABCs of EETCs – A Guide to Enhanced Equipment Trust Certificates*, Salomon Smith Barney, 8 June 2001, p. 37 (Exhibit BRA-71).

²¹⁴ http://www.southwest.com/about_swa/press/factsheet.html.

²¹⁵ <http://www.rati.com/airlines/AirlineFinance>. 1998 is the most recent year for which information regarding ASA is publicly available.

²¹⁶ Exhibit BRA-67.

²¹⁷ According to Brazil, many other factors in addition to sales revenues would enter into this calculus. Brazil uses sales revenue merely to illustrate that while companies' credit ratings may be equivalent, the terms at which the companies might obtain financing may not necessarily be so.

regional airlines have outperformed the majors in a number of key areas including revenue growth and, in terms of market capitalisation, a number of the regional airlines – including Comair and ASA – are the same size if not larger than some of the US majors. Canada therefore submits that Brazil is wrong to suggest that regional airlines should pay more for financing than the major US airlines simply because of their sales revenues.²¹⁸

7.253 Although Canada has addressed some of the concerns raised by Brazil, it has not responded to all of them. In particular, Canada has not responded to Brazil's observation that the 10-year general industrial corporate bonds represent simple averages at which bonds issued by a wide variety of companies in a wide variety of industries are trading at a given point in time. In the absence of compelling assurances by Canada that the difficulties identified by Brazil regarding the use of average data are misplaced, we do not consider it appropriate (especially given the availability of company-specific bond data submitted by Canada) to base our findings (for any of the EDC transactions at issue) on a comparison of the EDC's financing terms with average spreads offered in the general industrial corporate bond market.

Conclusion

7.254 We recall that the EDC's March 1997 offer to ASA was priced [], and that a [] interest rate constitutes evidence that the interest rate would be more favourable than rates available in the market, and in the absence of any counter-evidence, would justify a finding that such an interest rate confers a benefit.²¹⁹ Here, there is additional relevant evidence on market rates. While the EDC's March 1997 offer to ASA is priced [] the [] tranche of the [], it is priced [] the March 1997 spread for [].²²⁰ On balance we find that there is credible but conflicting evidence on whether the EDC's March 1997 offer was below market. Thus, on the basis of the evidence presented, we conclude that Brazil has failed to establish that the EDC's March 1997 offer to ASA was priced below market and conferred a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement.

(b) ASA – August 1998

7.255 The EDC offered financing to ASA in August 1998 at T plus [], for []. At that time, ASA was rated [] secured / [] unsecured by the EDC.

7.256 Brazil claims that the EDC's August 1998 offer to ASA confers a "benefit" because the repayment term exceeded the maximum authorised under the *OECD Arrangement*, and the spread offered by the EDC was [].

7.257 We recall our finding that a repayment term in excess of the 10-year period authorised by the *OECD Arrangement* is not positive evidence of "benefit" within the meaning of Article 1.1(b) of the SCM Agreement. We also recall, however, that the fact that an interest rate is [] constitutes evidence that the interest rate would be more favourable than rates available in the market, and in the absence of any counter-evidence on market rates, would justify a finding that such an interest rate confers a "benefit".²²¹

7.258 Canada has relied on a number of factors to demonstrate that the EDC's August 1998 offer to ASA was consistent with the market. Without referring to each and every factor identified by Canada, we first note that Canada has relied on the [] tranche of a [] issued in [] at T plus []. Although

²¹⁸ For a full description of Canada's arguments on this issue, see para. 7.207, *supra*.

²¹⁹ See para. 7.241 *supra*.

²²⁰ As to the weight to be given to individual company EETC data, we recall that both parties have expressed some reservations. See footnote 202, *supra*.

²²¹ See para. 7.241 *supra*.

there is no need for any credit rating adjustment, we recall that EETC's have generally been issued in respect of large aircraft, and that the EDC's offer should therefore be adjusted, i.e., reduced, by 20-30 basis points to a "large aircraft level". The adjusted EDC offer would be T + [], which is [] than the price of the [] tranche of the [] identified by Canada.

7.259 Second, we note that Canada relies on the price at which [] were trading in August 1998. Although these bonds were priced at T plus [] and [] respectively, i.e., in excess of the EDC offer, these [] were rated [] at that time, [] than ASA's unsecured rating of []. As noted above, Brazil has asserted that each notch may account for a difference of up to 15 basis points.²²² On this basis, the price of the [], adjusted [] to [] (i.e., reduced by [] basis points to T plus [] and []), would be [] than the EDC's August 1998 offer to ASA (i. e., T plus []).²²³ Canada has submitted evidence to the effect that adjusting a credit rating from [] to [] would result in a [] basis point reduction in interest rates.²²⁴ Such adjustment would reduce the price of the [] to T plus [] and [], again [] the EDC's August 1998 offer to ASA.

7.260 We recall that the EDC's August 1998 offer to ASA was priced [], and that a [] interest rate constitutes evidence that the interest rate would be more favourable than rates available in the market, and in the absence of any counter-evidence, would justify a finding that such an interest rate confers a benefit.²²⁵ Here, there is additional relevant evidence on market rates. While the EDC's August 1998 offer to ASA is priced [] the [] tranche of the [], it is priced [] the August 1998 spread for [].²²⁶ On balance we find that there is credible but conflicting evidence on whether the EDC's August 1998 offer was below market. Thus, on the basis of the evidence presented, we conclude that Brazil has failed to establish that the EDC's August 1998 offer to ASA was priced below market and conferred a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement.

(c) ACA – February 1996

7.261 The EDC issued an indicative term sheet (providing for financing at T plus []) to ACA in February 1996, when the EDC rated ACA [] secured / [] unsecured. No formal offer was made by the EDC at that time.

7.262 According to Brazil, "Canada defends its pricing of offers to [ACA] in part on the ground that one of its offers was ultimately not accepted by ACA. Brazil notes that whether or not EDC's early offers were accepted, EDC appears to have relied on its February 1996 offer to ACA in pricing EDC support for the Comair transaction. ... Thus, these offers provide further evidence that EDC does not follow market principles".²²⁷

7.263 In our view, there is no basis for us to make any findings regarding the February 1996 indicative term sheet. This term sheet was not binding on the EDC, and the terms therein would not necessarily have been reflected in any financing ultimately offered²²⁸ by the EDC to ACA. For these

²²² See para. 7.196, *supra*.

²²³ As noted above (See para. 7.247, *supra*), there is no need to adjust the EDC offer to take into account the type of aircraft at issue when comparing EDC's offer with [], since these are [] corporate bonds.

²²⁴ See Appendix 1 to Annex II of Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel (Annex B-12).

²²⁵ See para. 7.241 *supra*.

²²⁶ As to the weight to be given to individual company EETC data, we recall that both parties have expressed some reservations. See footnote 202, *supra*.

²²⁷ Comments of Brazil on Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel, para. 47 (Annex A-17).

²²⁸ Although Brazil refers to a February 1996 "offer", only an indicative term sheet was issued by the EDC at that time.

reasons, we find that the indicative term sheet is not a "financial contribution" within the meaning of Article 1.1(a) of the SCM Agreement.

7.264 The fact that the EDC may have referred to its February 1996 indicative term sheet for ACA in respect of pricing offered to Comair is without consequence. The fact that the indicative term sheet may have been referred to in respect of Comair may be relevant when reviewing the EDC's financing to Comair. However, that does not mean that it is of such a nature as to constitute a "financial contribution" to ACA.

(d) ACA – March 1999

7.265 In March 1999, the EDC offered ACA fixed rate financing at T plus [], or floating rate financing at LIBOR plus [], over []. At the time, the EDC rated ACA [] secured / [] unsecured.

7.266 Brazil submits that the EDC's offer was below market, because it was priced []. In its 13 August 2001 submission, Canada argues that the price at which [] was trading in March 1999 "does not provide a good 'on the run' benchmark" because it was "not frequently traded". Canada notes that this was the reason cited by SSB for excluding [] from its EETC database.²²⁹ In our view, the fact that an EETC is not frequently traded could be a valid reason for disregarding it for the purpose of establishing valid market benchmarks against which to compare the EDC's financing. In addition, we note that Brazil did not object to Canada's statement that the [] "does not provide a good 'on the run' benchmark". Accordingly, we draw no conclusions regarding the consistency with the market of the EDC's March 1999 offer to ACA on the basis of the price at which [] was trading at that time.

7.267 Brazil also asserts that the EDC's March 1999 offer to ACA was compared to the sale of a [] to [].²³⁰ In this regard, we note that Exhibit CAN-39, which contains the pricing strategy for an offer to Kendell, refers to the price of prior EDC loans to [] and ACA. The EDC therefore clearly took the price of an earlier loan to [] into account when pricing its loan to Kendell. However, this does not mean that the EDC also took its loan to [] into account for the purpose of its financing to ACA. We therefore do not see the relevance of Brazil's argument to our examination of the EDC's financing to ACA.²³¹

7.268 In order to demonstrate that the EDC's March 1999 offer to ACA is consistent with the market, Canada asserts, *inter alia*, that earlier financing offered by the EDC had only been used for the acquisition of [] by November 1999. Canada asserts that financing for other CRJs acquired by ACA came from a combination of []. Canada submits that the EDC was advised that the financing from [] in 1998 was priced at T plus [] over [].²³² The EDC was also advised that financing from [] was offered in early 1999 at Libor plus [] basis points, corresponding to approximately T plus [], based on November 1999 swap rates.²³³ We note that the EDC's March 1999 offer was less favourable than these offers from [] and [], which are commercial operators.

²²⁹ Exhibit CAN-81.

²³⁰ See Oral Statement of Brazil at the Second Meeting of the Panel, para. 104, referring to Exhibit CAN-39 (Annex A-12).

²³¹ We note that Canada has responded to Brazil's argument in the context of the EDC's financing to Kendell, and not in the context of the EDC's financing to ACA (See Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel, para. 18 (Annex B-12)).

²³² In its oral statement at the second meeting of the Panel, Brazil indicated [].

Brazil first made a claim regarding the EDC's March 1999 offer to ACA at the second meeting of the Panel. Documentary evidence regarding the EDC's March 1999 offer to ACA was therefore not covered by earlier requests by the Panel for documents / supporting evidence regarding EDC financing. However, there is no basis for us to doubt the veracity of Canada's assertions regarding financing offered by [].

²³³ Reference to the [] financing is contained in EDC documents submitted as Exhibit CAN-39.

7.269 Canada has also submitted evidence indicating that [] (then rated []) were trading at T plus [] and [] in March 1999. Since these [] are rated the same as the EDC's unsecured rating for ACA, there is no need for any credit rating adjustment when comparing the price of the EDC's offer with the price of the []. The EDC's March 1999 offer (i. e., T plus []) is [] than the price at which [] were trading in March 1999.

7.270 Although the EDC's offer was [] than the relevant [] pricing, other factors enumerated above indicate that the EDC's March 1999 offer to ACA was not made on terms more favourable than those available to ACA on the market. For this reason, we find that the EDC's March 1999 offer to ACA did not confer a "benefit".

(e) Comair – July 1996

7.271 The EDC offered Comair financing for [] aircraft in July 1996 at T plus [] basis points, for a period of []. The EDC rated Comair [] (secured) / [] (unsecured) at that time.

7.272 Brazil claims that the EDC's offer confers a "benefit", because it is []. Brazil also asserts that the offer was not consistent with commercial principles because the EDC took into account [].²³⁴

Minimum Lending Yield ("MLY")

7.273 Canada has submitted evidence indicating that the EDC's July 1996 offer was [] bps [] the EDC's MLY. According to the EDC Resolution Respecting MLYs, "[]".²³⁵ This would imply that EDC financing [].²³⁶ Canada has consistently argued in these proceedings that the EDC operates on commercial principles.²³⁷ Thus, we are entitled to presume that the EDC's definition of [] would be the same as that of a commercial lender. Accordingly, the fact that the EDC finances [], and therefore does not include [], would suggest that the EDC is financing below market, and therefore confers a "benefit". However, this conclusion should not be drawn if there is other specific evidence indicating that the financing at issue was not made available on terms more favourable than those available to the recipient on the market.

[]

7.274 Evidence submitted by Canada also demonstrates that, for the purpose of formulating its July 1996 offer to Comair, the EDC took into account [].²³⁸ In certain circumstances, the fact that the EDC provides financing on the basis of [] may suggest that the financing is not consistent with commercial principles, and therefore below market, since commercial lenders would be unlikely to take into account []. However, this conclusion would not be reached if there is other specific evidence that the financing is not more favourable than financing available to the recipient on the market.

²³⁴ See Exhibit CAN-59, p. 3.

²³⁵ See Exhibit CAN-47.

²³⁶ Canada has asserted that "the fixed margin for credit risk may be [] on the authority of the President or Senior Vice President Finance and Chief Financial Officer of EDC". According to Canada, "an authorized margin [] the identified fixed margin is the [] for that transaction". We have evidence that EDC offered financing [] to Comair in two transactions: in July 1996 and August 1997. None of the documentary evidence submitted by Canada regarding these transactions contains any details regarding the basis on which the President or Senior Vice President Finance and Chief Financial Officer of EDC may have authorised the [] of the fixed margin for credit risk. Nor does it contain any data indicating that any margin authorised by the President or Senior Vice President Finance and Chief Financial Officer of the EDC was [] for the two transactions at issue (See paras 6.13 and 6.14, *supra*).

²³⁷ First Written Submission of Canada, para. 19 (Annex B-4).

²³⁸ See Exhibit CAN-59, p. 3.

Market indicators submitted by Canada

7.275 Canada has submitted evidence that the EDC's July 1996 offer to Comair was less favourable than the general industrial index for bonds of the same credit rating (i.e., [] secured / [] unsecured). As noted above, however, we do not consider it appropriate to base our findings on data of such a general nature.

7.276 Canada has also provided evidence that [], rated [], were trading at T plus [] and [] in July 1996. There is no need for any credit rating adjustment to this price, since the [] were rated the same as Comair's unsecured rating. The EDC's offer (of T + []) to Comair is [] than the price of the [].²³⁹

7.277 Canada has also asserted that, at the time of the EDC's pricing of its July 1996 offer to Comair, there were "recent market pricing indications for Comair" of T plus [] and []. In particular, an Annex attached to an internal EDC memo dated 10 April 1996 includes the following passage:

Benchmarks:

1.[]²⁴⁰

Again, the EDC's July 1996 offer to Comair is priced [] these market indicators.

7.278 Thus, the above evidence submitted by Canada to demonstrate that the EDC's offer was consistent with the market, actually indicates that the EDC's July 1996 offer to Comair was made on terms more favourable than those available to Comair in the market. Although the abovementioned Annex also states that "[t]he [] banks have indicated an agreement with [the EDC's] pricing strategy"²⁴¹, we do not consider that this general assertion without reference to specific interest rates is sufficient to rebut the specific evidence submitted by Canada. In addition, we recall that the EDC's July 1996 offer is [], and that in making its offer the EDC considered []. On balance, therefore, we find that the EDC's July 1996 offer to Comair did confer a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement.

(f) Comair – December 1996 and March 1997

7.279 In December 1996 and March 1997, the EDC offered financing to Comair at T plus [] basis points, for []. Since Brazil has not made any specific arguments regarding these transactions, there is no basis for us to find that they confer a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement. In any event, we note that there is ample evidence to suggest that the EDC's December 1996 offer to Comair was priced above offers from commercial banks.²⁴²

(g) Comair – August 1997

7.280 In August 1997, the EDC offered Comair financing at T plus [] basis points, for [].

7.281 Brazil asserts that the EDC's offer conferred a "benefit" because it was [], and []. We recall that the fact that an interest rate is [] constitutes evidence that the interest rate would be more favourable than rates available in the market, and in the absence of any counter-evidence on market rates, would justify a finding that such an interest rate confers a "benefit".²⁴³ We also recall that EDC

²³⁹ At para. 7.209, we note that Canada calculated an *ex post* 1996 rating of [] for Comair. Adjusting the [] prices to reflect a [] rating would clearly result in EDC's offer being priced even lower than the [].

²⁴⁰ See Exhibit CAN-59, p. 4.

²⁴¹ See Exhibit CAN-59, p. 5.

²⁴² See Exhibit CAN-59, p. 6.

²⁴³ See para. 7.241 *supra*.

financing [] suggests the existence of a "benefit", although this conclusion should not be drawn if there is other specific evidence demonstrating that the EDC's offer is not more favourable than financing available to the recipient on the market.²⁴⁴

7.282 Thus, in order to rebut Brazil's claim of "benefit" on the basis of the two abovementioned factors, Canada should have adduced specific evidence indicating that the EDC's offer was not made on terms more favourable than those available to Comair in the market. Canada has failed to do so. Instead, Canada has submitted evidence containing a broad statement to the effect that in August 1997 "[m]arket interest in financing of the new Comair aircraft remain[ed] very strong, from []. As such, pricing [was] anticipated to be in the range of Treasuries plus [] basis points."²⁴⁵ This statement is not sufficient to rebut Brazil's claim of "benefit".

7.283 In light of the fact that the EDC's August 1997 offer to Comair was [] and [], and in the absence of specific evidence demonstrating that the EDC's offer was not made on terms more favourable than those available to Comair in the market, we find that the EDC's August 1997 offer to Comair conferred a "benefit".

(h) Comair – March 1998

7.284 In March 1998, the EDC offered Comair financing at [] plus [] basis points, for []. The EDC rated Comair [] secured / [] unsecured at that time.

7.285 Brazil asserts that the EDC's offer confers a "benefit", because the EDC's offer was [].²⁴⁶

7.286 The "comparables" referred to by Brazil are those set forth in Annex II of Canada's submission dated 13 August 2001. They include the general industrial index, the [] tranche of a []. As noted above, we do not consider it appropriate to base our findings on data submitted by Canada regarding the general industrial index. Regarding the [] tranche of the [], we note that it was issued in February 1998 at T plus []. The average rating of the split²⁴⁷ [] tranche is []²⁴⁸, which is []. We recall that, according to Brazil, [] may require a 15 basis point adjustment. This would lead to an adjusted [] price of T plus [] basis points, which is [] the EDC's offer to Comair.²⁴⁹ We further recall the need to increase EETC prices by 20-30 basis points, to arrive at an EETC price for regional aircraft transactions. The further adjusted [] price would be T plus [], which is [] than the EDC's offer to Comair.

7.287 The [] cited by Canada were rated [], some [] than the EDC's unsecured rating for Comair ([]). An adjustment must therefore be made before comparing the price of the [] with the EDC's March 1998 offer to Comair. If one assumes 15 basis points per notch, as Brazil has suggested²⁵⁰, the adjusted [] prices would be reduced by [] basis points, from T plus [] and [] to T plus [] and T plus []. Canada has submitted evidence to the effect that a change in rating from [] to [] would lead to a [] basis point spread reduction. Thus, using Canada's spread adjustment, the adjusted [] prices would be

²⁴⁴ See para. 7.273 *supra*.

²⁴⁵ See Exhibit CAN-59, p. 8.

²⁴⁶ Comments of Brazil on Responses of Canada to Questions and Additional Questions from the Panel Following the Second Meeting of the Panel, para. 42 (Annex A-16).

²⁴⁷ A company has a split rating when it is rated differently by Moody's and Standard & Poor's.

²⁴⁸ Canada submits that Moody's [] correlates to Standard & Poor's [] (*See* p. 12 of Annex II to Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel (Annex B-12)). This has not been disputed by Brazil.

²⁴⁹ Appendix 1 to Annex II of Canada's 13 August 2001 submission does not indicate what adjustment Canada considers would be appropriate to reflect a rating change of [] to [] (*See* Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel (Annex B-12)).

²⁵⁰ See para. 7.196, *supra*.

T plus [] and []. Using either Brazil's or Canada's adjustment, therefore, the adjusted [] prices would be lower, and more favourable, than the EDC's March 1998 offer to Comair.

7.288 Canada has also presented data regarding an [], rated [], and priced at T plus []. Canada notes that [] is not a commercial airline, and "therefore has less relevance in this analysis". Since [] is not a commercial airline, we do not consider that the price of its EETCs has any relevance for the purpose of reviewing the EDC's offers to commercial airlines.²⁵¹

7.289 Canada has also asserted that the EDC's March 1998 offer to Comair was deemed appropriate by the EDC "in comparison with ASA".²⁵² In this regard, we note that an internal EDC memo dated 10 March 1998 refers to a financing agreement "recently entered into" by the EDC with ASA. However, the record indicates that the only EDC financing to ASA in existence in March 1998 dates back to March 1997. We do not consider that the EDC's March 1997 financing to ASA is sufficiently contemporaneous for the purpose of reviewing the EDC's March 1998 offer to Comair.

7.290 We recall that the EDC's offer was priced [] favourably than the adjusted [] price, but [] favourably than the adjusted [] prices. We further recall the reservations expressed by both parties regarding the use of company-specific EETC data.²⁵³ On balance we find that there is credible but conflicting evidence on whether the EDC's March 1998 offer was below market. Thus, on the basis of the evidence presented, we conclude that Brazil has failed to establish that the EDC's March 1998 offer to Comair was priced below market and conferred a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement.

(i) Comair – February 1999

7.291 The EDC offered Comair [] financing at T plus []²⁵⁴ in February 1999, when the EDC rated Comair [] secured / [] unsecured.

7.292 Regarding the EDC's February 1999 offer to Comair, Brazil argued that the offer was below market because it was made at [] basis points above the EDC's cost of funds. It appears to us that this argument is based on the incorrect assumption that the offer was at T plus [] basis points, while we find the evidence demonstrates that the offer was made at T plus [] basis points and we will examine the transaction on that basis.²⁵⁵

7.293 Canada asserts that the EDC's pricing strategy considered a basket of US industrials including banks, industrials and consumer goods companies with a like credit rating and actively trading bonds with a similar term to maturity as the average life of the financing offered to Comair. According to Canada, the average spread on such bonds was T plus [] basis points, [] basis points lower than the

²⁵¹ See para. 7.216, *supra*.

²⁵² Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel, para. 76 (Annex B-12).

²⁵³ See footnote 202, *supra*.

²⁵⁴ Brazil has queried whether EDC's offer was T plus [] or T plus [], as the EDC recommendation contained in Exhibit CAN-59 refers to T plus []. Since the formal 26 February 1999 offer contained in Exhibit CAN-58 refers to T plus [], we see no reason to doubt Canada's assertion that the EDC's February offer was T plus []. Having assumed that the EDC's offer was actually T plus [], Brazil argued that the EDC's offer was below market because it was [] basis points above its cost of funds. Brazil did not state that this argument would apply equally in the event that the EDC actually offered T plus [] – or cost of funds plus 14 basis points (which Brazil merely compared with the general EETC market (*See* Oral Statement of Brazil at the Second Meeting of the Panel, para. 94 (Annex A-12)). Since we do not accept Brazil's suggestion that the EDC actually offered T plus [], we do not consider it necessary to address Brazil's argument that the EDC's offer was below market because it was [] basis points above its cost of funds.

²⁵⁵ *See* Oral Statement of Brazil at the Second Meeting of the Panel, para. 94 (Annex A-12).

EDC's February 1999 offer to Comair. Canada submits that the EDC [], the average spread of which (T plus [] basis points) was also lower than the EDC's February 1999 offer to Comair.

7.294 As noted above, we do not consider it appropriate to base our findings on average industrial bond spreads, especially when airline-specific benchmarks are available. Since Canada has adduced evidence regarding the [] tranche of a [], we shall base our findings on those indicators. The [] tranche of the [] was issued in [] at T plus []. This price would increase to T plus [] when one adds the 20 - 30 basis point regional aircraft premium. The EDC's offer is [] than the adjusted [] price.

7.295 [] were trading at T plus [] and [] in February 1999, when they were rated []. Since Comair was rated by the EDC as [] unsecured at that time, the price of the [] should be adjusted to reflect the [] difference in credit ratings. According to Brazil, a [] adjustment would cause the [] prices to decrease by [] basis points, to T plus [] and [], which is [] than the EDC's February 1999 T plus [] offer to Comair. According to evidence submitted by Canada, interest rates would decrease by [] basis points if a credit rating improved from [] to [].²⁵⁶ This would lead to an adjusted price of T plus [] and [] for [], which is also [] than the EDC's offer to Comair. Using both Brazil and Canada's adjustment methodologies, therefore, the adjusted [] prices are [] than the EDC's February 1999 offer to Comair.

7.296 Thus, the EDC's February 1999 offer to Comair is priced [] the [] tranche of the []. The EDC's offer is also priced [] the February 1999 spread for [].²⁵⁷ On the basis of the specific market evidence presented by Canada, therefore, we conclude that the EDC's February 1999 offer to Comair was more favourable than Comair could have obtained in the market. Accordingly, we find that the EDC's February 1999 offer to Comair did confer a "benefit".

(j) Kendell – August 1999

7.297 The EDC offered financing to Kendell in August 1999 at T plus [], for []. According to Canada, the EDC participated on an equal risk-sharing basis with seven other commercial lenders: []. Canada asserts that this was a commercial transaction, as the terms and conditions were dictated by the arranging banks [], and the financing was not conditional upon the EDC's participation. Canada asserts that the EDC was a price-taker, and not a price-maker, in this transaction. Canada also asserts that the EDC participated in this deal on a *pari passu* basis.

7.298 Brazil asserts that the EDC's offer to Kendell confers a "benefit" because the [] repayment term exceeds the maximum provided for in Article 21 of the *Sector Understanding on Export Credits for Civil Aircraft*. As noted above, Brazil has not established that a repayment term in excess of 10 years is necessarily more favourable than that available on the market. Accordingly, we decline to find the existence of a "benefit" on this ground.

7.299 Brazil also asserts that the transaction is not commercial, as alleged by Canada, since the fact that the EDC provided a large part of the financing means that this was an officially supported transaction. In this regard, Brazil queries whether the EDC participated in the transaction on a *pari passu* basis. Brazil also submits that Canada's assertion that the EDC financed [] per cent of the transaction is inconsistent with a statement in Exhibit CAN-39 that "[i]t is anticipated that EDC will fund up to []% of the notes while [] together with [] other identified underwriters, will hold the other []%". Brazil also states that Canada has provided no support for its assertion that the EDC was

²⁵⁶ See Appendix 1 to Annex II of Response of Canada to Oral Statement of Brazil at the Second Meeting of the Panel (Annex B-12).

²⁵⁷ As to the weight to be given to individual company EETC data, we recall that both parties have expressed some reservations. See footnote 202, *supra*.

merely a price-taker in this instance. In any event, Brazil submits that the EDC's presence in the deal necessarily affected the financing terms.

7.300 Dealing first with the extent of the EDC's participation in the Kendell August 1999 transaction, Canada has stated that the "EDC was responsible for [] percent, not [] percent of the lending provided".²⁵⁸ Canada has also asserted that, ultimately, [] banks also participated in the deal, alongside the EDC. It is clear, therefore, that the EDC's share of the financing was greater than that of at least some of the [] participating banks. According to Brazil, this means that the Kendell transaction was officially supported, rather than commercial. We do not agree. Provided the basic terms and conditions of the deal were fixed by commercial banks, and provided the EDC was exposed to the same risk of non-repayment of its loan as those commercial banks, we see no reason why this transaction should not be deemed to be commercial.

7.301 Brazil also asserts that the deal was not commercial because the EDC's presence necessarily affected the terms of the financing. We would only be able to accept this argument if it were clear that the banks' participation was dependent on participation by the EDC, or that the EDC was exposed to a greater risk (of default) than the participating banks. However, Canada has submitted that the deal was not dependent on the EDC's participation. According to Canada, the EDC was simply invited to participate as a price-taker. This is confirmed by evidence in the record.²⁵⁹ Furthermore, the EDC was exposed to the same risk of default as the participating banks.²⁶⁰ For these reasons, we reject Brazil's argument that the EDC's participation in the Kendell transaction necessarily affected the terms of the transaction.

7.302 Thus, in view of the fact that the terms and conditions of the financing provided by the EDC were arranged by commercial banks, and that the terms and conditions of the financing were not dependent on the EDC's participation, and since the EDC's exposure to the risk of repayment was the same as commercial banks, on balance we consider that this financing is on market terms, and not officially supported. We therefore find that the EDC's August 1999 financing to Kendell did not confer a "benefit".

(k) Air Nostrum

7.303 The EDC offered financing to Air Nostrum in October 1998, under both the Corporate Account and the Canada Account. The EDC's Corporate Account financing was priced at [] per cent (for []), whereas its Canada Account financing []. Financing was also provided under the *IQ* programme (at [] per cent).

7.304 Brazil asserts that the EDC's financing to Air Nostrum conferred a "benefit" because the weighted average interest rate for the deal ([] per cent) is [] for Deutschmark-denominated transactions ([]).

²⁵⁸ Oral Statement of Canada at the Second Meeting of the Panel, para. 50 (Annex B-10). The EDC's [] per cent participation is not inconsistent with the statement in Exhibit CAN-39 that "[i]t is anticipated that EDC will fund up to [] per cent" of the deal. Provided the EDC ultimately financed [] per cent or less of the deal, its participation is consistent with that statement.

²⁵⁹ See the Executive Summary contained in Exhibit CAN-37, whereby "[t]he Joint Arrangers/Underwriters are now seeking to offer to selected financial institutions the opportunity to buy Loan Notes to be issued under the Facility". Furthermore, the EDC Pricing Strategy contained in Exhibit CAN-39 states "[g]iven this pricing has already been committed, EDC, as participant, would be expected to accept pricing or stand aside".

²⁶⁰ This is evidenced by the fact that the EDC would share *pari passu* in the security (See Exhibit CAN-39).

7.305 According to Canada, Air Nostrum confirmed to the EDC that the Government of Brazil had offered long term financing for the Embraer contract, which was not consistent with *OECD Arrangement* terms. On the basis of this information, the EDC, with Canada Account support, provided a financing proposal which attempted to match the lease payment structure required by Air Nostrum but with a higher all-in rate than that being offered by Brazil. The EDC notified the OECD of its intention to match Brazil's offer. Canada submits that, though the overall pricing was driven by Canada's desire to match the Brazilian offer and to meet Air Nostrum's lease payment structure requirements, it was also based on a review of the airline's financial and operating performance.

7.306 In our view, it is not appropriate to analyse the EDC's financing to Air Nostrum on the basis of the weighted average of the interest rates payable to EDC Corporate Account, EDC Canada Account, and *IQ*, since Brazil has challenged each of these programmes (and specific transactions under these programmes) separately. Accordingly, the financing provided to Air Nostrum under each of these programmes should be examined separately. We examine the Canada Account and Corporate Account financing to Air Nostrum below.²⁶¹

7.307 As noted above, the EDC Canada Account financing to Air Nostrum was []. There is no question that an [] loan confers a "benefit", since such a loan would not be available on the market.²⁶²

7.308 With regard to the EDC's Corporate Account financing to Air Nostrum, Brazil's claim depends on finding that the weighted average interest rate was [] per cent, and therefore [] for Deutschmark-denominated transactions. As noted above, however, the rate charged by the Corporate Account was [] per cent, and we decline to analyse the EDC financing to Air Nostrum on the basis of a weighted average interest rate.²⁶³ Since Brazil has adduced no other transaction-specific arguments demonstrating that EDC's Corporate Account financing to Air Nostrum confers a "benefit", there is no basis for us to make such a finding.

Conclusion

7.309 For the above reasons, we find that financing provided under the EDC Corporate Account to ASA, ACA, Kendell, Air Nostrum and Comair in December 1996, March 1997, and March 1998 does not confer a "benefit", and therefore does not constitute a subsidy. It is therefore not necessary for us to consider whether or not the abovementioned EDC Corporate Account financing is "contingent ... upon export performance". However, we find that EDC Corporate Account financing to Comair in July 1996, August 1997 and February 1999 does confer a "benefit", and is therefore a subsidy. In addition, we find that the EDC's Canada Account financing to Air Nostrum is a subsidy. In order to determine whether or not these subsidies are prohibited export subsidies, we must consider whether or not the financing at issue is "contingent ... upon export performance".

3. Is the EDC's Corporate Account financing to Comair "contingent ... upon export performance"?

7.310 Brazil asserts that the EDC, which operates the Corporate Account programme, was "established for the purposes of supporting and developing, directly or indirectly, Canada's export

²⁶¹ Regarding the alleged *IQ* financing to Air Nostrum, see footnote 289.

²⁶² Although Canada has referred to the matching provisions of the *OECD Arrangement*, Canada has made no attempt to demonstrate that the Canada Account financing to Air Nostrum falls within the safe haven provided for in the second paragraph of item (k).

²⁶³ In any event, we recall our earlier finding that below-CIRR financing does not necessarily confer a "benefit" (See para. 7.241 *supra*).

trade and Canadian capacity to engage in that trade and to respond to international business opportunities".²⁶⁴

7.311 *First*, we note that Canada does not deny that the Corporate Account financing to Comair is "contingent ... upon export performance". *Second*, we consider that the above-mentioned statutory mandate of the EDC indicates that any financing it provides under the Corporate Account programme is necessarily "contingent ... upon export performance", since anything the EDC does is statutorily for the purpose of "supporting and developing ... Canada's export trade". For these reasons, we find that the Corporate Account financing to Comair is "contingent ... upon export performance".

4. Is the EDC's Canada Account financing to Air Nostrum "contingent ... upon export performance"?

7.312 Brazil asserts that the Canada Account offer to Air Nostrum is "contingent ... upon export performance" because "[t]he Canada Account is used to support export transactions", and because Canada Account is one way for the EDC to satisfy its "mandate to support and develop Canada's export trade and Canadian capacity to engage in that trade and to respond to international business opportunities"²⁶⁵.

7.313 In addressing Brazil's claim of export contingency, we note *first* that Canada does not deny that the Canada Account financing to Air Nostrum is "contingent ... upon export performance". *Second*, we note that Canada itself has stated that the mandate of the Canada Account is "to support and develop Canada's export trade and Canadian capacity to engage in that trade and to respond to international business opportunities".²⁶⁶ *Third*, we recall that the EDC, which operates the Canada Account programme, was "established for the purposes of supporting and developing, directly or indirectly, Canada's export trade and Canadian capacity to engage in that trade and to respond to international business opportunities".²⁶⁷ We therefore consider that any financing provided by the EDC under the Canada Account is necessarily "contingent ... upon export performance", since anything the EDC does is statutorily for the purpose of "supporting and developing ... Canada's export trade". *Fourth*, we note that the *Canada – Aircraft* panel found that the EDC Canada Account debt financing at issue in that case was "contingent ... upon export performance".²⁶⁸ For these reasons, we find that support provided under the Canada Account programme, including the financing to Air Nostrum, is "contingent in law ... upon export performance" within the meaning of Article 3.1(a) of the SCM Agreement.

5. Conclusion

7.314 To conclude, we find that financing provided under the EDC Corporate Account to ASA, ACA, Kendell, Air Nostrum and Comair in December 1996, March 1997 and March 1998 is not a subsidy.

7.315 We find, however, that the EDC's Corporate Account financing to Comair in July 1996, August 1997 and February 1999, and the EDC's Canada Account financing to Air Nostrum, take the form of subsidies that are "contingent ... upon export performance". We therefore find that the EDC's Corporate Account financing to Comair in July 1996, August 1997 and February 1999, and the EDC's Canada Account financing to Air Nostrum, are prohibited export subsidies, contrary to Article 3.1(a) of the SCM Agreement.

²⁶⁴ *Export Development Act*, footnote 42, *supra*, Section 10(1).

²⁶⁵ Industry Canada News Release, 10 January 2001(Exhibit BRA-3).

²⁶⁶ *Id.*

²⁶⁷ *Export Development Act*, footnote 42, *supra*, Section 10(1).

²⁶⁸ *See Canada – Aircraft*, Report of the Panel, footnote 35, *supra*, para. 9.230.

H. *IQ* EQUITY GUARANTEES

7.316 Brazil claims that a number of equity guarantees provided by *IQ* to airlines constitute prohibited export subsidies, contrary to Article 3.1(a) of the SCM Agreement. Brazil's claim concerns *IQ* equity guarantees provided to ACA (May 1997), Air Littoral (August 1997), Midway (July 1998), Mesa Air Group ("Mesa") (September 1998 and December 1999), Air Nostrum (January 1999), and Air Wisconsin (December 2000).²⁶⁹

7.317 Brazil claims that these *IQ* equity guarantees are subsidies because they are "financial contributions" that confer a "benefit". Brazil asserts that an *IQ* equity guarantee constitutes a "financial contribution" within the meaning of Article 1.1(a)(1)(i) and (iii) of the SCM Agreement. Brazil submits that an *IQ* equity guarantee confers a "benefit" because equity guarantees are not available in the market,²⁷⁰ and because they allow recipient airlines to pay less for equity than they would have to absent the *IQ* equity guarantee. Brazil submits that *IQ* equity guarantees are both *de jure* and *de facto* "contingent ... upon export performance".

7.318 Canada acknowledges that *IQ* equity guarantees constitute potential direct transfers of funds, and therefore "financial contributions", within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement. Canada denies that the *IQ* equity guarantees at issue confer a "benefit", however, because *IQ* charges market-based fees for those equity guarantees. Canada rejects Brazil's claim that *IQ* equity guarantees are either *de jure* or *de facto* "contingent ... upon export performance".

7.319 In order to examine Brazil's claim against the aforementioned *IQ* equity guarantees, we must determine whether or not *IQ* equity guarantees are "financial contributions" that confer a "benefit". If so, we must determine whether such *IQ* subsidies are "contingent ... upon export performance".

1. Are *IQ* equity guarantees "financial contributions"

7.320 The parties agree that *IQ* equity guarantees are "potential direct transfers of funds" within the meaning of Article 1.1(a)(1)(i). We see no reason to disagree, and therefore find that *IQ* equity guarantees are "financial contributions".²⁷¹

2. Do the *IQ* equity guarantees confer a "benefit"?

(a) Arguments of the parties

7.321 Brazil asserts that equity guarantees, otherwise known as first loss deficiency guarantees, do not appear to be available commercially. According to Brazil, Embraer has been informed that equity guarantees are not available in the market. In support, Brazil has submitted letters from two commercial banks.²⁷² Brazil submits that because *IQ* is offering something that the market does not provide, the provision of an equity guarantee by *IQ* is "quintessentially" a benefit.

²⁶⁹ Brazil initially alleged *IQ* support to Atlantic Southeast and Northwest (See First Written Submission of Brazil, para. 91 (Annex A-3)). However, Canada has denied any *IQ* or SDI involvement in those transactions (See Response of Canada to Question 38 from the Panel, Responses of Canada to Questions from the Panel Prior to the Second Meeting of the Panel (Annex B-9)).

²⁷⁰ See, for example, Response of Brazil to Question 53 from the Panel, Responses of Brazil to Questions from the Panel Prior to the Second Meeting of the Panel (Annex A-11).

²⁷¹ Since we have found that *IQ* equity guarantees are "financial contributions" on the basis of Article 1.1(a)(1)(i), there is no need for us to examine Brazil's claim that *IQ* equity guarantees constitute "financial contributions" by virtue of Article 1.1(a)(1)(iii).

²⁷² See Exhibit BRA-50.

7.322 Irrespective of the availability of equity guarantees in the market, Brazil submits that government guarantees to an equity investor protect that investor from the risks inherent in the equity market, and confer a "benefit" by making equity capital available to finance aircraft transactions on terms more favourable than would be the case in the market in the absence of the guarantee. Brazil asserts that, in order to demonstrate that there is no "benefit", Canada would have to prove that *IQ*'s fees are equal to those charged regional aircraft purchasers by commercial guarantors with A+ credit ratings. Furthermore, drawing on the logic of Article 14(c) of the SCM Agreement, Brazil asserts that there will be a "benefit" whenever a regional aircraft purchaser – which inevitably has a lower credit rating than the Government of Québec – receives an *IQ* equity guarantee, and there is a difference between the amount it pays for equity and the amount it would pay for equity absent the *IQ* guarantee.

7.323 Canada denies that *IQ* equity guarantees confer a "benefit" by providing something not available in the market. Canada asserts that equity guarantees are offered commercially in the market. Canada refers to evidence concerning the provision of equity guarantees by engine suppliers.²⁷³ Canada also refers to evidence regarding risk transfer instruments available in the market.

7.324 Canada asserts, on the basis of the Appellate Body report in *Canada – Aircraft*, that whether a benefit has been conferred can be determined by whether a recipient has received a financial contribution on terms more favourable than those available to it in the market. Canada notes the Appellate Body's finding that Article 14 of the SCM Agreement is relevant context in interpreting Article 1.1(b) and supports its view that the marketplace is an appropriate basis for comparison. According to Canada, however, there is no reason why Article 14(c) would be more relevant than any other part of Article 14, because Article 14(c) addresses loan guarantees, which are not at all equivalent to equity or first-loss deficiency guarantees. For Canada, the question of whether or not a "benefit" is conferred by *IQ* equity guarantees is a function of whether or not the recipient (*i.e.* the aircraft purchaser) obtains the financial contribution on terms more favourable than those available to it in the market.

7.325 Canada denies that *IQ* equity guarantees confer a "benefit", and accuses Brazil of failing to recognise that most guarantors, including *IQ*, charge fees for their guarantees.²⁷⁴ In particular, *IQ* receives both an up-front fee of [] basis points to cover its administrative costs, as well as an annual fee equivalent to [] basis points on its effective exposure.²⁷⁵

7.326 According to Canada, the market nature of the *IQ* guarantee can only be demonstrated by considering the value of the guarantee in light of the risk exposure of *IQ*. In this regard, Canada asserts that *IQ*'s risk exposure is greatly diminished [].²⁷⁶ Bombardier provides to *IQ* a counter-guarantee pursuant to which []. [] are more than adequate to compensate it for its risk and service.

7.327 Canada submits that the market nature of the annual fee is further demonstrated by the fact that, on average, Bombardier customers using *IQ* equity guarantees have chosen to do so on less than [] per cent of their unit volume. According to Canada, this proves that in practice, *IQ* provides financing services in competition with other financial institutions interested in participating in the

²⁷³ See, for example, Exhibit CAN-13.

²⁷⁴ Brazil has asserted that *IQ* Decree 1488-2000 eliminates fees as a condition for the grant of *IQ* equity guarantees. Canada denies this. The Panel does not consider it necessary to address this issue at this juncture, as we are not at present examining the *IQ* programme "as such". To the extent that Decree 1488-2000 relates to fees charged for any of the specific *IQ* transactions at issue, we shall examine that instrument when reviewing those specific transactions.

²⁷⁵ Bombardier counter-guarantees [].

²⁷⁶ Brazil queried whether such counter-guarantees are actually offered by Bombardier *per se*, or by Canadair Québec Capital ("CQC"), a company capitalized in equal parts by Bombardier and a company wholly-owned by *IQ*. Canada has confirmed that it is Bombardier, not CQC, that is responsible for the counter-guarantees. [].

aircraft financing market and that for the great majority of aircraft sold by Bombardier, the *IQ* guarantee is not sufficiently attractive to Bombardier's customers. In other words, the fact that [] per cent of the aircraft being financed are financed without *IQ* equity guarantees demonstrates that most of the time, Bombardier's customers are, at best, indifferent to *IQ* equity guarantees. For Canada, the necessary implication of these circumstances is that the fees charged by *IQ* in return for the guarantees are market rate; otherwise Bombardier's customers would not be so indifferent as to their availability.

7.328 Brazil asserts that whether or not Bombardier or some other entity provides [] counter-guarantees to *IQ* is irrelevant. By providing guarantees to the borrower, *IQ* facilitates more favourable financing terms because of Québec's superior credit rating, thus conferring a benefit. This is what "sweetens" the deal for the purchaser of Bombardier aircraft, and therefore, for Bombardier itself.

7.329 Brazil notes Canada's argument that, because [] per cent of the aircraft being financed are financed without *IQ* equity guarantees, Bombardier's customers are indifferent to *IQ* equity guarantees, and the fees charged by *IQ* in return for the guarantees are market rate. According to Brazil, Canada's logic is flawed, since the fact that [] per cent of the aircraft being financed are financed without *IQ* equity guarantees is irrelevant. Brazil asserts that what matters is the terms of *IQ* equity guarantees in the cases where they are provided, whatever the percentage of those cases is.

7.330 Furthermore, Brazil asserts that *IQ* has provided guarantees with no fees charged and, when it has charged fees, *IQ* uniformly charges a [] per cent fee, regardless of the credit ratings of the airlines involved. According to Brazil, it is hard to trace in this pattern any effort to follow a market. Brazil submits that no market guarantor would charge the same fee to recipients with varying credit ratings.

(b) Evaluation by the Panel

7.331 We shall first address Brazil's argument that *IQ* equity guarantees (also known as "first loss deficiency guarantees")²⁷⁷ "quintessentially" confer a "benefit" because *IQ* is providing something not available in the market. We shall then address Brazil's broader argument that *IQ* equity guarantees otherwise confer a "benefit" by making equity capital available to finance aircraft transactions on terms more favourable than would be the case in the market absent such guarantees.

(i) *Do IQ equity guarantees necessarily confer a "benefit" because equity guarantees are not available in the market?*

7.332 We shall begin by examining the factual issue of whether or not equity guarantees (also known as "first loss deficiency guarantees") are available in the market. Only if equity guarantees are not available in the market will we consider whether or not, as a matter of law, the provision by a government of support not available in the market necessarily confers a "benefit".

7.333 As a preliminary matter, we note that the two commercial bank letters submitted by Brazil do not state that equity guarantees are not available in the market. The first letter does not expressly refer to the availability of equity guarantees in the market. [] Thus, while both letters indicate that equity guarantees are "uneconomic", neither letter states categorically that equity guarantees are not available in the market.

²⁷⁷ We note that, in its request for the establishment of a panel, Brazil claims that "first loss deficiency guarantees", in addition to equity guarantees, provided by *IQ* are prohibited export subsidies (See WT/DS222/2).

7.334 We note that Canada has referred to the provision of equity guarantees by certain engine suppliers. Brazil submits that these guarantees were furnished by a participant in the sale, and not by a financial institution in the market. We agree with Brazil that the evidence adduced by Canada regarding the provision of equity guarantees to purchasers of aircraft by companies supplying the engines in the aircraft being purchased does not demonstrate that equity guarantees are available in the market.

7.335 Very late in these proceedings, in response to a question from the Panel at the second meeting, Canada also submitted evidence²⁷⁸ regarding the existence of a market for financial instruments that transfer risk in a manner similar to the equity guarantees provided by *IQ*. According to Canada, Bombardier has used private sector alternatives in precisely the same manner as *IQ*. []

7.336 Canada submits that, not only is this transaction analogous in structure to *IQ* guarantees, but the position in the financing and size of the [] tranche is identical to that of *IQ* in the vast majority of the latter's transactions. According to Canada, the only significant difference is that while the [] transaction was a [], the *IQ* structure features []. Canada submits that this has the effect of substantially lowering the risk assumed by the insurer (*IQ*).

7.337 Canada also submitted evidence²⁷⁹ which, in its view, shows that aircraft manufacturers can create innovative financing mechanisms centered around risk and remuneration. []

7.338 Canada has also submitted letters²⁸⁰ from two financial services institutions, indicating that there is an active private sector market for "risk transfer", the technical term for transactions of this kind. The first institution states that , []. The second institution states that [].

7.339 Brazil asserts that the evidence submitted by Canada does not demonstrate that Embraer would be able to find a guarantee equal to that offered by *IQ* in the market. With respect to the equity guarantee offered by a private insurer to Bombardier, Brazil notes that this guarantee is only for [] percent of the price of the aircraft for [], not the [] per cent for [] Embraer unsuccessfully offered Air Wisconsin, or the [] per cent for [] that Canada provided to Air Wisconsin through *IQ*. Brazil also notes that Canada failed to indicate the premium paid for the insurance, so there is no way to determine how the premium charged for this guarantee compared to the apparent [] per cent premium charged by *IQ*. Brazil asserts that the [] insurance programme only covers an apparent [] per cent effective guarantee through insurance, and notes that the cost of that guarantee has not been disclosed.

7.340 In light of the above, we consider that Canada has adduced sufficient evidence to establish the existence of equity guarantee-like instruments (including first loss deficiency guarantees) in the market. Brazil notes that the instruments identified by Canada have a different duration, and different coverage, than the *IQ* equity guarantees at issue. In our view, however, differences in duration and coverage do not negate a finding that equity guarantee-like instruments are available in the market.²⁸¹

7.341 Given the availability of equity guarantee-like instruments in the market, we find that there is no factual basis to Brazil's claim that *IQ* equity guarantees "quintessentially" confer a "benefit" because *IQ* is providing something that is not available in the market. For this reason, it is not necessary for us to consider whether or not, as a matter of law, the provision by a government of support not available in the market necessarily confers a "benefit".

²⁷⁸ See Exhibit CAN-74.

²⁷⁹ See Exhibit CAN-75.

²⁸⁰ See Exhibit CAN-76.

²⁸¹ Brazil also notes that Canada has not provided any evidence regarding the fees levied for these equity guarantee-like instruments. The question of fees is addressed at paras 7.348-7.357.

(ii) *Do IQ equity guarantees otherwise confer a "benefit"?*

7.342 In addressing this issue, we must first identify the appropriate method for determining whether or not *IQ* equity guarantees confer a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement. We start by recalling the findings of the panel and Appellate Body in *Canada – Aircraft*. In that case, the panel found that

a financial contribution will only confer a "benefit", *i.e.*, an advantage, if it is provided on terms that are more advantageous than those that would have been available to the recipient on the market.²⁸²

7.343 The Appellate Body upheld the findings of the panel, ruling that

the marketplace provides an appropriate basis for comparison in determining whether a "benefit" has been "conferred", because the trade-distorting potential of a "financial contribution" can be identified by determining whether the recipient has received a "financial contribution" on terms more favourable than those available to the recipient in the market.²⁸³

7.344 Consistent with the findings of the panel and Appellate Body in *Canada – Aircraft*, we consider that *IQ* equity guarantees will confer a "benefit" to the extent that they are made available to Bombardier customers on terms more favourable than those on which such Bombardier customers could obtain comparable equity guarantees in the market. We note that the parties appear to agree that this standard can be applied by reviewing the fees²⁸⁴, if any, charged by *IQ* for providing its equity guarantees.²⁸⁵ We agree that the "benefit" standard could be applied to *IQ* equity guarantees in this manner. Thus, to the extent that *IQ*'s fees are more favourable than fees that would be charged by guarantors with Québec's credit rating in the market for comparable transactions, *IQ*'s equity guarantees may be deemed to confer a "benefit".

7.345 We note Brazil's argument that even if *IQ*'s fees are equal to those charged regional aircraft purchasers by commercial guarantors with A+ credit ratings, under Article 14(c) of the SCM Agreement there would still be a "benefit" as long as there is a difference between the amount the purchaser pays for equity using an *IQ* equity guarantee and the amount it would pay for equity absent the *IQ* equity guarantee. Canada queries the relevance of Article 14(c) in this context, since that provision is concerned with "benefit" in the context of loan guarantees, rather than equity guarantees. In our view, although Article 14(c) is expressly concerned with "benefit" in the context of loan guarantees, there are perhaps sufficient similarities between the operation of loan guarantees and equity guarantees for it to be appropriate to rely on Article 14(c) for the purpose of establishing the existence of "benefit" in the context of equity guarantees in certain circumstances. Thus, a "benefit" could arise if there is a difference between the cost of equity with and without an *IQ* equity guarantee, to the extent that such difference is not covered by the fees charged by *IQ* for providing the equity guarantee. In our opinion, it is safe to assume that such cost difference would not be covered by *IQ*'s fees if it is established that *IQ*'s fees are not market-based.

²⁸² *Canada – Aircraft*, Report of the Panel, footnote 35, *supra*, para. 9.112.

²⁸³ *Canada – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 157.

²⁸⁴ For example, Brazil asserts that, in order to demonstrate that there is no "benefit", Canada would have to prove that *IQ*'s fees are equal to those charged regional aircraft purchasers by commercial guarantors with A+ credit ratings. For its part, Canada (although it rejects Brazil's argument regarding the burden of proof) asserts that there is no "benefit" because the annual fees for *IQ* equity guarantees are market-based.

²⁸⁵ We note that *IQ* purports to levy both an up-front [] per cent administrative fee, and an annual fee of [] per cent on *IQ*'s effective exposure. We do not understand Brazil to raise any claims regarding the up-front administrative fee. We understand that Brazil's claims are concerned only with the annual fee allegedly levied by *IQ*.

(iii) *Burden of proof*

7.346 Having established the proper "benefit" test to be applied in respect of *IQ* equity guarantees, we consider it important to clarify which party bears the burden of proof in respect of that standard. Brazil asserts that Canada bears the burden to prove that *IQ* equity guarantees do not confer a "benefit" (by proving that *IQ*'s fees are equal to those charged to regional aircraft purchasers by commercial guarantors with A+ credit ratings). Canada asserts that the burden is on Brazil to prove that *IQ* equity guarantees do confer a benefit.

7.347 It is now well established that the initial burden lies on the complaining party, which must establish a prima facie case of inconsistency. The burden then shifts to the defending party, which must counter or refute the claimed inconsistency.²⁸⁶ In order to demonstrate that the *IQ* equity guarantees confer a "benefit", the initial burden therefore lies on Brazil, as the complaining party, to demonstrate that any fees levied by *IQ* are more favourable than those that would be charged by equity guarantors in the market. We therefore reject Brazil's argument that, in order to demonstrate that there is no "benefit", Canada would initially have to prove that *IQ*'s fees are equal to those charged regional aircraft purchasers by commercial guarantors with A+ credit ratings.

(iv) *Application of the "benefit" standard to specific IQ transactions*

7.348 We shall now determine whether or not Brazil has demonstrated that any of the *IQ* equity guarantees at issue confer a "benefit". In this regard, we note Brazil's arguments that *IQ* equity guarantees confer a "benefit" either because they are provided free of charge, or because any fees levied by *IQ* are below market.

No fees charged

7.349 In its oral statement at the Panel's second substantive meeting with the parties, Brazil claimed that *IQ* has provided guarantees with no fees charged, "[a]s [Brazil] will show below in our discussion of specific transactions".²⁸⁷ Brazil did not indicate precisely which specific transaction(s) it was referring to in this regard. We have carefully reviewed the remainder of Brazil's oral statement, and consider that the only portion that could be interpreted as a claim of *IQ* providing an equity guarantee without charge is [], concerning the [] transaction. Since Brazil has not clearly identified any additional transactions where *IQ* allegedly provided equity guarantees without levying any fee, we shall address Brazil's argument (that *IQ* provides equity guarantees free of charge) by examining whether or not *IQ* charged fees for its equity guarantee to [].^{288, 289}

²⁸⁶ See *European Communities – Hormones*, Report of the Appellate Body, footnote 45, *supra*.

²⁸⁷ Oral Statement of Brazil at the Second Meeting of the Panel, para. 23 (Annex A-12).

²⁸⁸ In its written submission of 20 August 2001, Brazil asserts that for transactions for which Canada has shown evidence of a fee, it has only shown the [] basis point up-front administrative fee, and not the [] basis point annual fee Canada claims is also charged (*See* Comments of Brazil on Responses of Canada to Questions and Additional Questions from the Panel Following the Second Meeting of the Panel (Annex A-16)). [].

²⁸⁹ Oral Statement of Brazil at the Second Meeting of the Panel, para. 110 (Annex A-12). In para. 106 of that submission, Brazil submits that the evidence provided by Canada suggests that *IQ* also provided [], in addition to the equity guarantee. In para. 61 of its 20 August 2001 comments on Canada's 13 August 2001 submission, Brazil notes that Canada does not deny the provision of [] (*See* Comments of Brazil on Responses of Canada to Questions and Additional Questions from the Panel Following the Second Meeting of the Panel (Annex A-16)). While we accept that the documentary evidence presented by Canada appears to indicate the existence of [], Brazil has made no attempt to assert that such [] constitutes a subsidy. Thus, even if *IQ* did provide [], we have no basis on which to make any findings against such []. Brazil has requested adverse inferences regarding *IQ* support to certain airlines (including []) more generally. We address this issue below.

7.350 Brazil claims that, according to the summary of the transaction provided by Canada, *IQ* provided both an equity guarantee and []. According to Brazil, "the fee for the guarantee provided by CQC – [] percent – appears to have been [] for the transaction. Depending on how you look at it, therefore, either the guarantee was provided []. Canada does not respond to this argument.

7.351 The documentary evidence regarding the [] transaction is contained in Exhibit CAN-77.²⁹⁰ In a table describing the details of the transaction, provision is made for a [] per cent annual fee. [].²⁹¹ We are in no doubt – and Canada has not argued – that equity guarantees would not be provided in the market []. Since the *IQ* equity guarantee to [] was therefore provided on terms more favourable than [] could have obtained in the market, we find that the *IQ* equity guarantee to [] confers a "benefit".

Below-market fees

7.352 Brazil asserts that *IQ*'s annual fees are below-market because they are levied uniformly, at [] per cent, regardless of the credit ratings of the airlines involved.

7.353 Canada disagrees, on the basis of []. According to Canada, in large part the risk represented by the possible default of a particular aircraft purchaser is []. Canada asserts that, [], it is entirely appropriate that the fee charged to different purchasers would be the same.

7.354 Brazil raises two counter-arguments. First, Brazil asserts that Bombardier counter-guarantees may well reduce *IQ*'s risk exposure, but they are between Bombardier and *IQ*, and not between Bombardier and the purchaser. []. Second, Brazil asserts that []. Thus, *IQ*'s risk exposure is not diminished with respect to the remaining [] (or []) per cent of its guarantee.

7.355 In support of its argument that uniform fees are necessarily below-market, Brazil asserts that "[n]o market guarantor would charge the same fee to recipients with wildly varying credit ratings".²⁹² While we agree that market operators would normally charge different equity guarantee fees to customers with different credit ratings, to reflect the different degrees of risk exposure, it is theoretically possible that a uniform fee could be set in such a manner that it covers the risk exposure resulting from the provision of equity guarantees to customers with the lowest credit ratings. For

Brazil also claims that *IQ* provided financing to Midway, and that Canada has failed to provide full information regarding the terms of the *IQ* equity support to Midway. Brazil therefore requests an adverse inference in respect of the *IQ* equity guarantee to Midway. Canada denies that *IQ* provided financing to Midway, and suggests that Brazil confused the equity guarantee with direct financing. Given Canada's denial, and since we do not see anything in Exhibit CAN-61 that would indicate the existence of *IQ* financing to Midway, we see no basis for Brazil's assertion that *IQ* provided financing to Midway. Furthermore, Brazil has failed to specify why, in its view, Canada has failed to disclose full information regarding the *IQ* equity guarantee to Midway. For our part, we do not see what additional information should have been provided by Canada. We therefore reject Brazil's request for an adverse inference regarding the *IQ* equity guarantee to Midway.

Brazil also asked the Panel to draw an adverse inference regarding *IQ*'s equity guarantee to ACA, again alleging that Canada failed to provide full information regarding the terms of that transaction. We assume that Brazil is referring to the fact that Exhibit CAN-63 does not identify the creditor providing debt financing. In our view, however, the fact that Canada has failed to disclose the identity of the loan creditor has no bearing on the consistency of the *IQ* equity guarantee with the SCM Agreement. We therefore reject Brazil's request for an adverse inference regarding the *IQ* equity guarantee to ACA.

²⁹⁰ Canada initially submitted details of the first approval of the *IQ* equity guarantee to [] in Exhibit CAN-64. Canada subsequently informed the Panel that the first approval did not reflect the final terms and conditions of *IQ*'s offer, which were then submitted as Exhibit CAN-77.

²⁹¹ In response to Question 47 from the Panel, Canada asserted that "*IQ* has charged fees for every transaction in which it has participated and has provided for fees in every financing offer it has made" (Responses of Canada to Questions from the Panel Prior to the Second Meeting of the Panel (Annex B-9)). []

²⁹² Oral Statement of Brazil at the Second Meeting of the Panel, para. 23 (Annex A-12).

example, if market operators normally charge a two per cent fee to customers with CCC credit ratings, and a 0.25 per cent fee to customers with AAA+ ratings, the levying of a uniform two per cent fee would not necessarily indicate the existence of a "benefit". Instead, a "market" fee would effectively be charged to CCC recipients, while an above-market fee would be charged to AAA+ recipients. For this reason, we are unable to accept Brazil's argument that uniform fees are necessarily below-market.

7.356 Brazil could have sought to establish the existence of a "benefit" by producing evidence to the effect that the levying of a uniform [] fee (on *IQ*'s remaining [] per cent exposure) is not sufficient to cover the risk to which *IQ* is exposed when providing equity guarantees to airlines with the lowest credit ratings. Brazil might have done this, for example, with the assistance of the two financial institutions that provided the letters contained in Exhibit BRA-50. Both financial institutions asserted that the provision of equity guarantees of the sort offered by *IQ* would be uneconomic. In making these assertions, these institutions would presumably have made a preliminary estimation of the nature of the fee that would have to be charged when providing such equity guarantees. This preliminary estimation may have been useful in assessing whether or not the uniform [] fee levied by *IQ* is sufficient to cover the risk exposure resulting from the provision of equity guarantees to airlines with the lowest credit ratings. Brazil presented no such evidence, however. We note that we do not accept Canada's argument that the [] totally eliminate *IQ*'s exposure. Thus, to offer such guarantees on a market basis, *IQ* would still need to concern itself with the credit ratings of the beneficiaries of its guarantees. Nonetheless, it seems clear that the existence of [] would make it possible for *IQ* (or for a commercial bank or insurer) to charge a much lower fee (based on market considerations) than would otherwise be the case. In these circumstances, we cannot conclude that *IQ*'s uniform fee is necessarily a below-market fee for the beneficiaries with the lowest credit ratings. To do so, we would need some evidence of the market fees for these or similar guarantees, and we have none.

7.357 In light of the above, we find that Brazil has failed to establish its claims that the fee-based *IQ* equity guarantees confer a "benefit" and that the levying of a uniform fee for *IQ* equity guarantees necessarily confers a "benefit".

Conclusion

7.358 To conclude, we recall our finding that the *IQ* equity guarantee to Air Nostrum conferred a "benefit", and therefore constituted a subsidy. We also recall our finding that Brazil has failed to establish that the remaining *IQ* equity guarantees at issue conferred a "benefit", and therefore reject Brazil's claims against those remaining *IQ* equity guarantees. In order to determine whether or not the *IQ* equity guarantee to [] is a prohibited export subsidy, we must now consider whether or not it is "contingent ... upon export performance" within the meaning of Article 3.1(a) of the SCM Agreement.

3. Are *IQ* equity guarantees "contingent ... upon export performance"?

(a) Arguments of the parties

7.359 Brazil asserts that the *IQ* equity guarantees at issue are both *de jure* and *de facto* "contingent ... upon export performance". Regarding *de jure* export contingency, Brazil relies on the arguments it made in support of its claim that the *IQ* programme "as such" is "contingent ... upon export performance".²⁹³ Thus, Brazil refers to Section 25 of the *IQ Act*, which specifies "export activities" as one of the missions of *IQ*. Brazil also refers to *IQ* Decrees 572-2000 and 841-2000. Brazil notes that Decree 572-2000 enables *IQ* to provide financial support for investment projects or export projects, including the sale of goods outside of Québec, and that Decree 841-2000 grants *IQ* the authority to

²⁹³ Second Written Submission of Brazil, para. 148 (Annex A-10).

support market development projects, including projects ultimately focused on the sale of goods outside of Québec.

7.360 Regarding de facto export contingency, Brazil relies on the findings of the *Australia – Leather* panel.²⁹⁴ Brazil cites para. 9.67 of that panel's report to argue that a Member's awareness that its domestic market is too small to absorb domestic production of a subsidised product indicates the subsidy is granted on the condition that it be exported. In this regard, Brazil notes that [] per cent of Bombardier's regional aircraft have been sold outside of Canada, and that [] per cent of the regional aircraft transactions receiving *IQ* support have been for export outside of Canada.²⁹⁵

7.361 Brazil also asserts that Canada failed to provide certain documentation requested by the Panel that would have indicated whether or not the *IQ* equity guarantees at issue were contingent on export. Brazil submits that Canada's failure to provide that documentation should lead the Panel to draw adverse inferences regarding the export contingency of the *IQ* equity guarantees at issue.

7.362 Canada denies that any of the *IQ* equity guarantees at issue are "contingent ... upon export performance". In response to Brazil's arguments regarding *de jure* export contingency, Canada asserts that the legal basis for *IQ* financing for aircraft sales is Section 28 – not 25 – of the *IQ Act*. Canada asserts that Section 28 is used for many types of projects, whether or not they have export potential. Canada also asserts that Decrees 572-2000 and 841-2000 have nothing to do with aircraft sales financing and are not used for aircraft sales financing. In any event, Canada asserts that the term "exportation" in Decree 572-2000 refers to the sale of goods outside of Québec, and not outside of Canada.

7.363 Regarding Brazil's claim of de facto export contingency, Canada asserts that Brazil's reference to the panel's finding in *Australia – Leather* is both inaccurate and taken out of context. In particular, Canada considers that Brazil implies incorrectly that the *Australia – Leather* panel considered a Member's awareness that its market could not absorb subsidised domestic production to be sufficient to prove de facto export contingency. In fact, Canada argues, the subsidy in that case was conditioned in part on sales performance targets. Since the Australian government was aware of the fact that the recipient of the subsidy would have to maintain or increase export sales in order to meet those sales performance targets, the panel considered that those sales performance targets were in fact export performance targets. Canada also refers to the *Canada – Aircraft* proceedings, in which the Appellate Body found that it is not sufficient for a complainant alleging de facto export contingency to "demonstrate solely that a government granting a subsidy *anticipated* that exports would result".²⁹⁶

7.364 Regarding Brazil's request for adverse inferences, Canada asserts that, to the best of its knowledge, it has provided all of the documentation that exist regarding the review of the *IQ* equity guarantee transactions.

(b) Evaluation by the Panel

7.365 We shall begin by addressing Brazil's claim that the *IQ* equity guarantees at issue are *de jure* "contingent ... upon export performance". In this regard, we are guided by the finding of the Appellate Body in *Canada – Autos* that a subsidy is *de jure* conditional on export performance "when

²⁹⁴ *Australia – Subsidies Provided to Producers and Exporters of Automotive Leather*, Report of the Panel, WT/DS126/R, adopted 16 June 1999.

²⁹⁵ See Responses of Canada to Questions 19 and 20 from the Panel, Responses of Canada to Questions from the Panel Following the First Meeting of the Panel (Annex B-7).

²⁹⁶ *Canada – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 171 (emphasis in original).

the existence of that condition can be demonstrated on the basis of the very words of the relevant legislation, regulation, or other legal instrument constituting the measure".²⁹⁷ Furthermore, in *Canada – Aircraft* the Appellate Body stated that "the ordinary connotation of 'contingent' is 'conditional' or 'dependent for its existence on something else'".²⁹⁸

7.366 Brazil asserts that the *de jure* export contingency of the *IQ* equity guarantees at issue results from Section 25 of the *IQ Act*, and from Decrees 572-2000 and 841-2000. First, we note Canada's assertion that the legal basis for the guarantees at issue was actually Section 28 of the *IQ Act*, and not Section 25 as initially alleged by Brazil. Brazil appears to have accepted that "*IQ* guarantees to regional aircraft purchasers were issued pursuant to [Section] 28" of the *IQ Act*.²⁹⁹ Section 28 of the *IQ Act* provides

The Government may, where a project is of major economic significance for Québec, mandate [*IQ*] to grant and administer the assistance determined by the Government to facilitate the realization of the project. The mandate may authorize the agency to fix the terms and conditions of the assistance.

7.367 We see nothing in the words of Section 28 of the *IQ Act* to suggest that *IQ* equity guarantees based on that provision are *de jure* export contingent. Nor has Brazil argued that Section 28 of the *IQ Act* demonstrates export contingency.^{300 301}

7.368 Regarding Decrees 572-2000 and 841-2000, we note that these legal instruments entered into force in June 2000. With the exception of the Air Wisconsin transaction, all of the *IQ* equity guarantees at issue were provided before June 2000. Furthermore, Brazil itself has asserted that the legal basis for the *IQ* equity guarantee to Air Wisconsin was Decree 1488-2000,³⁰² and not Decree 572-2000 and / or 841-2000. Since none of the *IQ* equity guarantees at issue were provided on the

²⁹⁷ *Canada – Certain Measures Affecting the Automotive Industry* ("*Canada – Autos*"), Report of the Appellate Body, WT/DS139/AB/R-WT/DS142/AB/R, adopted 19 June 2000, para. 100.

²⁹⁸ *Canada – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 166.

²⁹⁹ See Second Written Submission of Brazil, para. 120 (Annex A-10).

³⁰⁰ Brazil relies on Section 25 of the *IQ Act* to establish the *de jure* export contingency of *IQ* equity guarantees. Section 25 sets forth the "mission" of *IQ*. Even if *IQ* equity guarantees were provided on the basis of Section 25, we do not consider that Section 25 would necessarily render such guarantees *de jure* export contingent. Brazil has relied on that part of the *IQ* mission dealing with the "[g]rowth of enterprises", described in Section 25 as including "export activities". Without finding that this part of the *IQ* mission would demonstrate *de jure* export contingency, we note that the *IQ* mission set forth in Section 25 also includes, for example, "[s]upport to enterprises", whereby *IQ* "shall also work to retain current investment in Québec by providing support to enterprises established in Québec that show particular dynamism or potential". In our view, there is nothing in the latter description of *IQ*'s mission that would suggest export contingency. Furthermore, even if the *IQ* guarantees at issue were provided on the basis of Section 25, there is nothing to suggest that they were necessarily provided as part of the "[g]rowth of enterprises", rather than "[s]upport to enterprises". We have already stated our view that that part of *IQ*'s mission regarding "[s]upport to enterprises" would not suggest export contingency. Accordingly, even if Section 25 were the legal basis for the *IQ* guarantees at issue, that fact alone would not necessarily mean that they were *de jure* export contingent.

³⁰¹ To the extent that para. 131 of the Appellate Body's report on *Canada – Autos* (on the use of domestic over imported goods) requires an examination of the actual operation of a statute to determine whether or not there is *de jure* export contingency, we note that we have found no aspect of the operation of the *IQ Act* in specific transactions that would suggest export contingency (See our findings on *de facto* export contingency below).

³⁰² See Second Written Submission of Brazil, paras. 110 and 118 (Annex A-10).

basis of Decrees 572-2000 and / or 841-2000, the wording of those instruments could not render the *IQ* equity guarantees at issue *de jure* export contingent.³⁰³

7.369 For these reasons, we find that the *IQ* equity guarantees at issue are not *de jure* "contingent ... upon export performance".

7.370 In addressing Brazil's de facto export contingency claim, we shall be guided by note 4 to Article 3.1(a) of the SCM Agreement, whereby a subsidy is "contingent ... in fact ... upon export performance" when

the facts demonstrate that the granting of a subsidy, without having been made legally contingent upon export performance, is in fact tied to actual or anticipated exportation or export earnings. The mere fact that a subsidy is granted to enterprises which export shall not for that reason alone be considered to be an export subsidy within the meaning of this provision.

7.371 Brazil's de facto export contingency claim is based on its interpretation of the findings of the *Australia – Leather* panel. That panel found that

the Australian market for automotive leather is too small to absorb Howe's production, much less any expanded production that might result from the financial benefits accruing from the grant payments, and the required capital investments, which were to be specifically for automotive leather operations.* Therefore, we conclude that, in order to expand its sales in a manner that would enable it to reach the sales performance targets (interim targets and the aggregate target) set out in the grant contract, Howe would, of necessity, have to continue and probably increase exports. At the time the contract was entered into, the government of Australia was aware of this necessity, and thus anticipated continued and possibly increased exports by Howe. In our view, these facts effectively transform the sales performance targets into export performance targets. We thus consider that Howe's anticipated export performance was one of the conditions for the grant of the subsidies. Australia argues that this consideration would lead to a result that would penalize small economies, where firms are often dependent on exports in order to achieve rational economic levels of production. Nevertheless, in the specific circumstances of this case, we find this consideration compelling evidence of the close tie between anticipated exportation and the grant of the subsidies.³⁰⁴ (* footnote omitted)

7.372 According to the *Australia – Leather* panel, therefore, in certain circumstances (in the presence of export performance targets, for examples) a Member's awareness that its domestic market is too small to absorb domestic production of a subsidised product may indicate that the subsidy is granted on the condition that it be exported. In this regard, we note that *IQ* was very likely aware that the Canadian domestic market was too small to absorb Bombardier production, because [] per cent of Bombardier's regional aircraft have been sold outside of Canada, and [] per cent of the regional aircraft transactions receiving *IQ* support have been for export outside of Canada.

7.373 However, in *Canada – Aircraft*, the Appellate Body stated that

³⁰³ In the context of Brazil's claim against the *IQ* programme "as such", the parties disagreed as to whether or not Decrees 572-2000 and 841-2000 could be used for providing *IQ* support for regional aircraft transactions. Since Decrees 572-2000 and 841-2000 are not relevant to the *IQ* equity guarantees at issue, we do not consider it necessary to resolve this issue.

³⁰⁴ *Australia – Leather*, Report of the Panel, footnote 294, *supra*, para. 9.67.

169. ... satisfaction of the standard for determining *de facto* export contingency set out in footnote 4 requires proof of three different substantive elements: first, the "granting of a subsidy"; second, "is ... *tied to* ..."; and, third, "actual or anticipated exportation or export earnings". (emphasis added) We will examine each of these elements in turn.

170. The first element of the standard for determining *de facto* export contingency is the "granting of a subsidy". In our view, the initial inquiry must be on whether the *granting authority* imposed a condition based on export performance in providing the subsidy. ...

171. The second substantive element in footnote 4 is "tied to". The ordinary meaning of "tied to" confirms the linkage of "contingency" with "conditionality" in Article 3.1(a). Among the many meanings of the verb "tie", we believe that, in this instance, because the word "tie" is immediately followed by the word "to" in footnote 4, the relevant ordinary meaning of "tie" must be to "limit or restrict as to ... conditions".* This element of the standard set forth in footnote 4, therefore, emphasises that a relationship of conditionality or dependence must be demonstrated. The second substantive element is at the very heart of the legal standard in footnote 4 and cannot be overlooked. In any given case, the facts must "demonstrate" that the granting of a subsidy is *tied to* or *contingent upon* actual or anticipated exports.* It does *not* suffice to demonstrate solely that a government granting a subsidy *anticipated* that exports would result. The prohibition in Article 3.1(a) applies to subsidies that are *contingent* upon export performance.

172. We turn now to the third substantive element provided in footnote 4. The dictionary meaning of the word "anticipated" is "expected".* The use of this word, however, does *not* transform the standard for "contingent ... in fact" into a standard merely for ascertaining "expectations" of exports on the part of the granting authority. Whether exports were anticipated or "expected" is to be gleaned from an examination of objective evidence. This examination is quite separate from, *and should not be confused with*, the examination of whether a subsidy is "tied to" actual or anticipated exports. A subsidy may well be granted in the knowledge, or with the anticipation, that exports will result. Yet, that alone is not sufficient, because that alone is not proof that the granting of the subsidy is *tied to* the anticipation of exportation.

173. There is a logical relationship between the second sentence of footnote 4 and the "tied to" requirement set forth in the first sentence of that footnote. The second sentence of footnote 4 precludes a panel from making a finding of *de facto* export contingency for the sole reason that the subsidy is "granted to enterprises which export". In our view, merely knowing that a recipient's sales are export-oriented does not demonstrate, without more, that the granting of a subsidy is tied to actual or anticipated exports. The second sentence of footnote 4 is, therefore, a specific expression of the requirement in the first sentence to demonstrate the "tied to" requirement. We agree with the Panel that, under the second sentence of footnote 4, the export orientation of a recipient may be taken into account as *a* relevant fact, provided that it is one of several facts which are considered and is not the only fact supporting a finding. (* footnotes omitted)

7.374 Thus, even if a Member were to anticipate that exports would result from the grant of a subsidy (because, for example, of the export-orientation of the recipient), the Appellate Body has made it clear that such anticipation "alone is not proof that the granting of the subsidy is *tied to* the anticipation of exportation" within the meaning of note 4 to Article 3.1(a).

7.375 In upholding the findings of the *Canada – Aircraft* panel, the Appellate Body noted that

the Panel took into account sixteen different factual elements, which covered a variety of matters, including: TPC's statement of its overall objectives; types of information called for in applications for TPC funding; the considerations, or eligibility criteria, employed by TPC in deciding whether to grant assistance; factors to be identified by TPC officials in making recommendations about applications for funding; TPC's record of funding in the export field, generally, and in the aerospace and defence sector, in particular; the nearness-to-the-export-market of the projects funded; the importance of projected export sales by applicants to TPC's funding decisions; and the export orientation of the firms or the industry supported.³⁰⁵

7.376 On a general level, a number of the factors identified by the Appellate Body may be relevant in the present case, particularly in respect of *IQ*'s "overall objectives",³⁰⁶ *IQ*'s "record of funding in the export field", "the nearness-to-the-export-market of the projects funded", and "the export orientation of the firms or the industry supported". In considering "the nearness-to-the-export-market of the projects funded", we note the Appellate Body's statement that "[i]f a panel takes this factor into account, it should treat it with considerable caution. In our opinion, the mere presence or absence of this factor in any given case does not give rise to a presumption that a subsidy is or is not *de facto* contingent upon export performance".³⁰⁷ In considering "the export orientation of the firms or the industry supported", we recall the Appellate Body's finding that a Member's awareness that the grant of a subsidy may result in exports – because, for example, of the export orientation of the recipient firm or industry – "alone is not proof that the granting of the subsidy is *tied to* the anticipation of exportation" within the meaning of note 4 to Article 3.1(a).

7.377 With regard to the "overall objectives" of *IQ*, and its "record of funding in the export field", we see important differences between the operation of the TPC programme and the operation of the *IQ* programme. In particular, we note that TPC employees were required to focus on the volume of export sales resulting directly from the project. There is no evidence to suggest that this was the case in respect of *IQ* support. In addition, TPC Business Plans recorded the proportion of the aerospace and defence industry's revenue allocable to exports. Again, there is nothing to suggest that *IQ* focused on the proportion of revenue allocable to exports. Furthermore, while the 1996-1997 TPC Annual Report stated that "[t]he 12 largest firms [in the A&D sector] account for most of the R&D and shipments, of which 80 per cent are exported",³⁰⁸ only [] per cent of total *IQ* support has directly or indirectly concerned Bombardier regional aircraft (all of which were exported outside of Canada).³⁰⁹ In other words, while TPC was clearly operated in a way that suggests that TPC support was "tied to" anticipated exports, there is no evidence in the record to suggest that *IQ* is operated in a similar manner.

7.378 In light of the above, we are not persuaded that *IQ* equity guarantees are *de facto* export contingent.³¹⁰

³⁰⁵ *Canada – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 175.

³⁰⁶ We note that part of *IQ*'s mission is to "participate in the growth of enterprises, in particular by facilitating research and development and export activities" (Section 25, *IQ Act* (Exhibit BRA-18)).

³⁰⁷ *Canada – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 174.

³⁰⁸ *Canada – Aircraft*, Report of the Panel, footnote 35, *supra*, para. 9.340.

³⁰⁹ See Response of Canada to Questions 18 and 19 from the Panel, Responses of Canada to Questions from the Panel Following the First Meeting of the Panel (Annex B-7).

³¹⁰ We recall that, according to footnote 4 to Article 3.1(a) of the SCM Agreement, "[t]he mere fact that a subsidy is granted to enterprises which export shall not for that reason alone be considered to be an export subsidy".

7.379 Brazil has also asked the Panel to draw adverse inferences regarding the alleged export contingency of the *IQ* equity guarantees at issue. Brazil's request is based on the alleged failure by Canada to provide all the documentation requested by the Panel in its Question 14 to Canada, dated 29 June 2001. Question 14 reads:

Brazil has identified a number of *IQ* transactions in paragraphs 90 and 91 of its first written submission. Canada has not denied that *IQ* was involved in any of these transactions. Please provide full details of the terms and conditions of these transactions. Please also provide all documentation regarding the review of these transactions by *IQ*. Please also provide the credit ratings of the relevant airlines at the time of these transactions.

7.380 In its response to Question 14, Canada asserted that *IQ* has been involved with only two of the Bombardier customers identified by Brazil in its first written submission. Canada informed the Panel of three additional airlines, not identified by Brazil, to which *IQ* had provided equity guarantees. While Canada provided details of the terms and conditions of these *IQ* transactions, it failed to provide any "documentation regarding the review of these transactions by *IQ*". Accordingly, on 20 July 2001, we addressed the following Question 41 to Canada:

Please provide the documentation requested in Question 14 from the Panel, particularly in respect of the specific guarantee fees involved, [], or explain why such documentation is not available.

In addition, please provide all documentation regarding the review by *IQ* of the Air Littoral, Atlantic Coast Airlines and Air Nostrum transactions referred to in Canada's response to Question 14 from the Panel.

7.381 In its response to our Question 41, Canada provided documentary evidence regarding *IQ*'s review of the relevant transactions. Subsequently, in response to Question 71 from the Panel, Canada informed us that the documentation it provided in respect of the *IQ* equity guarantee to Air Nostrum did not reflect the final terms and conditions of that guarantee. It therefore submitted documents regarding the final terms and conditions, apologising for the "error" and stating that it "was not previously aware of the existence of the second set of documents for this transaction". In response to Question 72 from the Panel, Canada then asserted that, "[t]o the best of its knowledge, Canada has provided all of the documentation that exists regarding the review of these transactions by *IQ*".

7.382 Brazil made the following comment on Canada's response to Question 72 from the Panel:

In its response to Question 72, Canada states that it "has provided all of the documentation that exists" regarding *IQ*'s review of the Mesa, Midway, Air Littoral, Atlantic Coast Airlines, and Air Nostrum transactions. This response is highly suspect in light of the conflicting answers and documentation that Canada has produced to the Panel involving the Air Nostrum sale. Brazil asks the Panel to consider the following points.

On 29 June 2001, the Panel asked Canada, in Question 14, to "provide full details of the terms and conditions" of *IQ*'s support for certain aircraft sales, and "all documentation regarding the review of these transactions by *IQ*." On 6 July 2001, Canada responded, in part, by firmly stating that *IQ* was only involved in the Air Nostrum deal to the extent that it provided an "equity guarantee" of up to a maximum of []% of the aircraft purchase price." However this statement conflicts with the summary of the Air Nostrum transaction that appears in Exhibit [CAN]-64, a document that Canada withheld until 26 July 2001.

Exhibit [CAN]-64 contains [].

Instead of disclosing to the Panel this discrepancy, Canada now simply states that Exhibit [CAN]-64 "did not reflect the final terms and conditions of the guarantee provided by IQ". Instead, in response to Question 71, Canada now provides a new document, Exhibit [CAN]-77, dated 18 June 1998. Canada states that this document contains IQ's "final recommendation and transaction summary" for Air Nostrum. The "Détails du Financement" chart provided with Exhibit [CAN]-77 indicates that the percentages contained in Exhibit [CAN]-64 have changed. [].

Although the percentages and terms contained in Exhibit [CAN]-77 differ from Exhibit [CAN]-64 only slightly, Brazil notes that they differ significantly from those in Canada's response to Question 14. More importantly, however, the appearance of Exhibit [CAN]-77 at this late stage in this dispute is extremely troubling, and casts a cloud on Canada's statement that "it has provided all of the documentation that exists regarding the review" of this and other transactions by IQ. Canada states that it "was not previously aware of the existence" of Exhibit [CAN]-77. If this is true, then one must question whether the documents that Canada has provided regarding IQ do, in fact, represent IQ's final recommendations for the Mesa, Midway, Air Littoral, Atlantic Coast Airlines, and Air Nostrum transactions. This is particularly true in light of Canada's initial statement in response to Question 14 that IQ only provided an "equity guarantee" to Air Nostrum. Brazil therefore asks the Panel to take adverse inferences and presume that other documents exist that show that subsidies contingent on export have been granted.

7.383 We understand Brazil's request for adverse inferences to be based on two considerations. *First*, because Canada failed to disclose the provision of *IQ* financing to Air Nostrum. *Second*, because of doubts as to whether Canada has submitted the final recommendations regarding the *IQ* equity guarantees to Mesa Air Group, Midway, Air Littoral, ACA and Air Nostrum.

7.384 Regarding the first point, we note that the request we addressed to Canada in our Question 14, and which we repeated in Question 41, did not specifically include *IQ* financing. Our requests referred to the *IQ* transactions identified by Brazil in paragraphs 90 and 91 of its first written submission, which only concerned equity guarantees. Thus, although one might have hoped that Canada would be more forthcoming,³¹¹ Canada was not required to provide details of *IQ* financing in order to respond fully to Questions 14 and 41.³¹² Furthermore, we do not understand Canada to have

³¹¹ In this regard, we note Article 3.10 of the DSU which enjoins Members of the WTO, if a dispute arises, to engage in dispute settlement procedures "in good faith in an effort to resolve the dispute". As the Appellate Body has previously stated, the "procedural rules of WTO dispute settlement are designed to promote, not the development of litigation techniques, but simply the fair, prompt and effective resolution of trade disputes" (*United States – Tax Treatment of "Foreign Sales Corporations"*, Report of the Appellate Body, WT/DS108/AB/R, adopted 20 March 2000, para. 166).

³¹² Strictly speaking, our request for documentation was limited to the *IQ* transactions identified by Brazil in its first written submission. Nevertheless, in responding to our question, Canada also referred to three additional *IQ* transactions not identified by Brazil in its first written submission. That being said, we regret that it was necessary for us to address a second request for documentary evidence to Canada, in the form of Question 41 from the Panel (*See Responses of Canada to Questions from the Panel Prior to the Second Meeting of the Panel (Annex B-9)*). Canada has offered no explanation as to why such documentary evidence, which was not supplied with respect to those transactions identified by the Panel or with respect to additional transactions revealed by Canada, could not have been included in its initial response to Question 14 from the Panel (*See Responses of Canada to Questions from the Panel Following the First Meeting of the Panel (Annex B-7)*). We do believe, however, that it was appropriate for us to request the documentation a second

stated that *IQ* "only" provided an equity guarantee to Air Nostrum. While Canada stated that *IQ* had provided an equity guarantee to Air Nostrum, it did not exclude the possibility that other forms of *IQ* support had also been provided. Again, Canada's response to our questions, which were based on Brazil's first written submission, did not require it to disclose the existence of *IQ* financing to Air Nostrum.

7.385 Regarding the second point, we are not persuaded that an "error" on the part of Canada regarding the final terms and conditions of the *IQ* equity guarantee to Air Nostrum should cause us to doubt whether Canada has provided details of the final terms and conditions of the *IQ* equity guarantees to Mesa Air Group, Midway, Air Littoral, ACA and Air Nostrum. Canada has assured us that "[t]o the best of its knowledge, Canada has provided all of the documentation that exists regarding the review of these transactions by *IQ*". We see no reason to doubt Canada's assurance.

7.386 In light of the above, we do not consider it appropriate to draw the inference requested by Brazil.

4. Conclusion

7.387 To conclude, while we find that the *IQ* equity guarantee to [] is a subsidy, we find that it is neither *de jure* nor *de facto* "contingent ... upon export performance", within the meaning of Article 3.1(a) of the SCM Agreement. Accordingly, we reject Brazil's claim that the *IQ* equity guarantee to [] is a prohibited export subsidy.

7.388 Since we have found that the remaining *IQ* equity guarantees at issue do not confer a "benefit", we also reject Brazil's Article 3.1(a) claims against those measures.

I. *IQ* LOAN GUARANTEES

7.389 Brazil has made claims against loan guarantees provided by *IQ* to Mesa Air Group (September 1998 and December 1999), and to the EDC in respect of the Air Wisconsin transaction (December 2000).

(a) Arguments of the parties

7.390 Brazil asserts that loan guarantees are *per se* prohibited by item (j) to the Illustrative List of Export Subsidies.³¹³ An *IQ* loan guarantee constitutes a "financial contribution" within the meaning of Article 1.1(a)(1)(i) and (iii) of the SCM Agreement. An *IQ* loan guarantee confers a benefit by substituting a superior governmental credit rating for a borrower's inferior credit rating. The loan guarantee confers a "benefit" by enabling an airline to borrow funds based upon the credit rating of the Government of Québec, which is A+ or A2. To demonstrate that the *IQ* loan guarantees at issue are "contingent ... upon export performance", Brazil invokes the same arguments that it relied on in respect of the abovementioned *IQ* equity guarantees.

7.391 Canada acknowledges that *IQ* loan guarantees constitute "financial contributions". In particular, they constitute potential direct transfers of funds or liabilities within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement. In particular Canada denies that the *IQ* loan guarantees at issue confer a "benefit", however, because *IQ* charges market-based fees for those loan guarantees. Canada rejects Brazil's claim that *IQ* loan guarantees are "contingent ... upon export performance", for the same reasons as Canada denied the export contingency of *IQ* equity guarantees.

time, rather than simply reject Canada's answer as incomplete or unresponsive, as Brazil seemed to suggest we should do.

³¹³ See Second Written Submission of Brazil, para. 112 (Annex A-10).

(b) Evaluation by the Panel

7.392 We shall first examine whether or not *IQ* loan guarantees are "financial contributions" that confer a "benefit". If, as a result, we find that *IQ* loan guarantees constitute subsidies, we shall then consider whether or not such subsidies are "contingent ... upon export performance" within the meaning of Article 3.1(a).

7.393 We note that Canada acknowledges that *IQ* loan guarantees constitute "financial contributions" within the meaning of Article 1.1(a)(1)(i) of the SCM Agreement. We agree and there is therefore no need for us to examine this matter further.³¹⁴

7.394 Brazil argues that loan guarantees are *per se* prohibited by item (j) to the Illustrative List of Export Subsidies. Item (j) provides:

(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 the long-term operating costs and losses of the programmes.

7.395 In our view, item (j) sets out the circumstances in which the grant of loan guarantees is *per se* deemed to be an export subsidy (i.e., when the "premium rates ... are inadequate to cover the long-term operating costs and losses" of the loan guarantee). Item (j) certainly does not provide, as alleged by Brazil, that all loan guarantees are *per se* prohibited by item (j). Since Brazil has made no attempt to argue that the *IQ* loan guarantees at issue were provided "at premium rates which are inadequate to cover the long-term operating costs and losses" thereof, we make no findings against the *IQ* loan guarantees at issue on the basis of item (j) of the Illustrative List of Export Subsidies.³¹⁵

7.396 Brazil also asserts that the *IQ* loan guarantees at issue necessarily confer a "benefit" by enabling the relevant airlines to borrow funds based upon the superior credit rating of the Government of Québec, which is A+ or A2. This argument essentially means that any government loan guarantee necessarily confers a "benefit" (since the very purpose of a government loan guarantee is to make available the superior credit rating of the government concerned). We are unable to accept this argument, since it ignores the clear distinction made in Article 1.1 of the SCM Agreement between a "financial contribution" and a "benefit".³¹⁶ The term "benefit" relates to the effects of a "financial contribution". Thus, in order to demonstrate the existence of a "benefit", a complaining party must do more than establish the existence of a "financial contribution".

7.397 In considering precisely what Brazil must show in order to demonstrate the existence of a "benefit", we note the findings of the panel and Appellate Body in *Canada – Aircraft*. We therefore consider that *IQ* loan guarantees will confer a "benefit" to the extent that they are made available to Bombardier customers on terms more favourable than those on which such Bombardier customers could obtain comparable loan guarantees in the market. In applying this standard, we are guided by Article 14(c) of the SCM Agreement, which provides contextual guidance for interpreting the term

³¹⁴ In particular, there is no need for us to consider whether or not *IQ* loan guarantees constitute the provision of "goods or services other than general infrastructure" within the meaning of Article 1.1(a)(1)(iii) of the SCM Agreement, as alleged by Brazil.

³¹⁵ We also note that neither party has sought to rely on an *a contrario* reading of item (j) for the purpose of demonstrating, or refuting, the existence of "benefit".

³¹⁶ Brazil's argument also ignores the terms of Article 14(c), which explains the circumstances in which government loan guarantees "shall not be considered as conferring a benefit" in the context of countervailing duty investigations. If all government loan guarantees necessarily conferred a "benefit", as argued by Brazil, the Article 14(c) guideline would be meaningless.

"benefit" in the context of loan guarantees.³¹⁷ Article 14(c) provides that, for the purpose of calculating the amount of a subsidy in terms of the "benefit" to the recipient (for the purpose of a countervailing duty investigation):

(c) a loan guarantee by a government shall not be considered as conferring a benefit, unless there is a 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. In this case the benefit shall be the difference between these two amounts adjusted for any differences in fees;

7.398 In our view, and taking into account the contextual guidance afforded by Article 14(c), we consider that an *IQ* loan guarantee will confer a "benefit" when "there is a difference between the amount that the firm receiving the guarantee pays on a loan guaranteed by [*IQ*] and the amount that the firm would pay on a comparable commercial loan absent the [*IQ*] guarantee. In this case the benefit shall be the difference between these two amounts adjusted for any differences in fees". In other words, there will be a "benefit" when the cost-saving for a Bombardier customer for securing a loan with an *IQ* loan guarantee is not offset by *IQ*'s fees. In our opinion, it is safe to assume that this will be the case if it is established that *IQ*'s fees are not market-based.

7.399 In applying this "benefit" test to the two *IQ* loan guarantees at issue, we note Brazil has made no arguments to the effect that "there is a difference between the amount that the [Mesa Air Group] pays on a loan guaranteed by [*IQ*] and the amount that the [Mesa Air Group] would pay on a comparable commercial loan absent the [*IQ*] guarantee", adjusted for any difference in fees. In particular, although Brazil does not deny that loan guarantees are available on a commercial basis, Brazil has failed to adduce any arguments or information regarding what Mesa Air Group might have had to pay on a comparable commercial loan absent the *IQ* loan guarantee.³¹⁸ Nor has Brazil made any other argument to the effect that *IQ*'s fee for its loan guarantee to Mesa Air Group is not market-based. Accordingly, we reject Brazil's claim that the *IQ* loan guarantee to Mesa Air Group confers a "benefit".

7.400 Regarding the *IQ* loan guarantee to the EDC in respect of the Air Wisconsin transaction, Brazil has asserted (in a letter dated 3 September 2001, commenting on certain documentary evidence submitted by Canada at the request of the Panel) that *IQ* "charged [] for this guarantee". As noted above, it is safe to assume that there is "a 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", adjusted for any differences in fees, if the relevant fees are not market-based. There is no doubt that a fee of [] is not market-based, because a market operator would not provide a loan guarantee [].

7.401 [] In fact, the evidence before us suggests that the *IQ* loan guarantee to the EDC is []. In a table summarising the equity and loan guarantees to be provided by *IQ* in respect of the Air Wisconsin transaction, [].

7.402 In light of the evidence before us, which suggests that the *IQ* loan guarantee for the Air Wisconsin transaction is [], and in light of the contextual guidance afforded by Article 14(c) of the SCM Agreement, we find that the *IQ* loan guarantee to the EDC for the Air Wisconsin transaction

³¹⁷ See *Canada – Aircraft*, Report of the Appellate Body, footnote 35, *supra*, para. 155, regarding the contextual relevance of Article 14 for the purpose of determining the existence of "benefit".

³¹⁸ We recall that the initial burden lies on the complaining party to establish a *prima facie* case of inconsistency (See para. 7.75, *supra*).

confers a "benefit" within the meaning of Article 1.1(b) of the SCM Agreement, and therefore constitutes a subsidy.

7.403 In order to determine whether or not the *IQ* loan guarantee for the Air Wisconsin transaction constitutes a prohibited export subsidy, we must consider whether or not the loan guarantee is "contingent ... upon export performance". We note that Brazil's claim regarding the export contingency of *IQ* loan guarantees is based on the same arguments as those advanced in support of its claim regarding the export contingency of *IQ* equity guarantees. Since we have already found that Brazil's arguments do not demonstrate that the *IQ* equity guarantees at issue in these proceedings are "contingent ... upon export performance", we are compelled to make the same finding in respect of *IQ*'s loan guarantees. Accordingly, we find that the *IQ* loan guarantee to the EDC for the Air Wisconsin transaction is not "contingent ... upon export performance" within the meaning of Article 3.1(a) of the SCM Agreement.

(c) Conclusion

7.404 We find that the *IQ* loan guarantee to Mesa Air Group is not a subsidy, since it does not confer a "benefit" within the meaning of Article 1.1(b). We find that the *IQ* loan guarantee to Air Wisconsin is a subsidy, but that it is not "contingent ... upon export performance". For these reasons, we reject Brazil's claim that the *IQ* loan guarantees to Mesa Air Group and Air Wisconsin constitute prohibited export subsidies, contrary to Article 3.1(a) of the SCM Agreement.

VIII. CONCLUSIONS AND RECOMMENDATION

8.1 In conclusion, we:

- (a) reject Brazil's claim that the EDC Corporate Account and Canada Account programmes "as such" constitute prohibited export subsidies contrary to Article 3.1(a) of the SCM Agreement;
- (b) reject Brazil's claim that the *IQ* programme "as such" constitutes a prohibited export subsidy contrary to Article 3.1(a) of the SCM Agreement;
- (c) reject Brazil's claim that the EDC Corporate Account and Canada Account programmes "as applied" constitute prohibited export subsidies contrary to Article 3.1(a) of the SCM Agreement;
- (d) reject Brazil's claim that the *IQ* programme "as applied" constitutes a prohibited export subsidy contrary to Article 3.1(a) of the SCM Agreement;
- (e) uphold Brazil's claim that the EDC Canada Account financing to Air Wisconsin constitutes a prohibited export subsidy contrary to Article 3.1(a) of the SCM Agreement;
- (f) uphold Brazil's claim that the EDC Canada Account financing to Air Nostrum constitutes a prohibited export subsidy contrary to Article 3.1(a) of the SCM Agreement;
- (g) uphold Brazil's claim that the EDC Corporate Account financing to Comair in July 1996, August 1997 and February 1999 constitutes a prohibited export subsidy contrary to Article 3.1(a) of the SCM Agreement;

- (h) reject Brazil's claim that the EDC Corporate Account financing to ASA, ACA, Kendall Air Nostrum and Comair in December 1996, March 1997 and March 1998 constitutes a prohibited export subsidy contrary to Article 3.1(a) of the SCM Agreement;
- (i) reject Brazil's claim that *IQ* equity guarantees to ACA, Air Littoral, Midway, Mesa Air group, Air Nostrum and Air Wisconsin constitute prohibited export subsidies contrary to Article 3.1(a) of the SCM Agreement; and
- (j) reject Brazil's claim that *IQ* loan guarantees to Mesa Air Group and Air Wisconsin constitute prohibited export subsidies contrary to Article 3.1(a) of the SCM Agreement.

8.2 Pursuant to Article 3.8 of the DSU, the findings in sub-paragraphs (e), (f) and (g) of the preceding paragraph also constitute a case of *prima facie* nullification or impairment of benefits accruing to Brazil under the SCM Agreement, which Canada has not rebutted.

8.3 In light of the above findings, we are required to make the recommendation provided for in Article 4.7 of the SCM Agreement. Accordingly, we recommend that Canada withdraw the subsidies identified above without delay.

8.4 Article 4.7 further provides that "the panel shall specify in its recommendation the time-period within which the measure must be withdrawn." In other words, we are required to specify what period would represent withdrawal "without delay". Taking into account the procedures that may be required to implement our recommendation on the one hand, and the requirement that Canada withdraw its subsidies "without delay" on the other, we conclude that Canada shall withdraw the subsidies identified in sub-paragraphs (e), (f), and (g) of paragraph 8.1 within 90 days.
