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WTO LEGAL IMPACTS ON COMMODITY SUBSIDIES

GREEN BOX OPPORTUNITIES IN THE FARM BILL FOR FARM INCOME THROUGH THE CONSERVATION AND CLEAN ENERGY DEVELOPMENT PROGRAMS

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INTRODUCTION AND SUMMARY OF CONCLUSIONS

This memorandum[1] examines the applicability of World Trade Organization ("WTO") agreements regarding subsidies to the farm-assistance programs contained in Titles II and IX of the Farm Security and Rural Investment Act of 2002, 7 U.S.C. § 7911, et seq.[2] The focus of the analysis is whether conservation and renewable energy and energy efficiency payments to U.S. farmers are "green box" programs and thus exempt from reductions on agricultural subsidies that the United States and other countries have agreed to as part of an effort to reduce aggregate levels of so-called "amber box" subsidies. Stated slightly differently: Does it matter for the purposes of international law and WTO-related international commitments what proportion of the total United States government subsidies are paid to farmers in the form of conservation and renewable energy and energy efficiency payments, as opposed to the many other forms of farm subsidies, especially commodity payments, that are used by the United States government? The short answer is "yes."

This memorandum presents three principal conclusions:

(1) Strict textualism dominates the interpretation of WTO agreements in the dispute resolution process, and a strict textualist reading of the Agricultural Agreement supports placement of Unites States conservation and renewable energy and energy efficiency payments into the "green box" with two exceptions: (a) Those conservation payments, if any, that more than compensate farmers for the cost of implementing conservation practices; and (b) Those payments to producers of bioenergy where the production input is an agricultural commodity that is grown and marketed by other WTO members, such as wheat, corn or soybeans. These two types of payments likely qualify as amber box payments and may be subject to limits on such payments agreed to by WTO members (including the United States). Although not technically "green box" payments, payments to producers of cellulosic ethanol are not limited by the GATT/WTO framework because animal and plant wastes are not agricultural commodities that are the subject of international trade.

(2) Although all energy efficiency and renewable energy payments to farmers under Title IX and related clean energy provisions likely qualify as green box payments, those payments that provide and leverage the greatest environmental benefits are most assured to withstand challenge to their green box status.

(3) There is an open question on how to reconcile the Subsidies and Countervailing Measures Agreement ("SCM Agreement"), which does not contain any explicit exemption from challenges to green box subsidies (except for a very limited exemption for one-time subsidies to ease compliance costs with new environmental regulations), and the Agricultural Agreement,

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[2] Most of the energy efficiency and renewable energy programs enacted as part of the 2002 Farm Bill appear in the new Title IX "Energy Title," but several of the new provisions were adopted through amendments to programs in Title II (Conservation), Title VI (Rural Development) and Title VII (Research).

which places green box placements in a privileged, protected category. The question of reconciling the SCM Agreement and the Agricultural Agreement vis-à-vis green box subsidies may well be decided by multilateral negotiations, in which case the political dynamics would seem to support continued protection of green box subsidies. The same result will likely occur if the issue is treated, instead, as purely a matter of legal interpretation of the current SCM and Agricultural Agreement texts, in which case the WTO Appellate Body would decide the issue. Given the greater specificity of the Agricultural Agreement vis-à-vis agricultural goods as compared with the SCM Agreement, which is cast in broad terms, and the WTO's commitment to sustainable development as an interpretive prism, the Agricultural Agreement will likely be read by WTO decisionmakers as trumping the SCM Agreement in the absence of any new WTO agreements to the contrary. This should be true at least with respect to those green box subsidies that can be understood as primarily aimed at the achievement of sustainable development. Subject to the two exceptions noted above, the conservation and renewable energy and sustainable energy payments by the United States government to farmers qualify as green box payments, and because those payments plainly do advance sustainable development policies, those payments should not be vulnerable to a challenge based on the SCM Agreement.

The memorandum is organized as follows. Part I provides a brief overview of relevant WTO authorities and terms. Part II develops the argument that a straightforward textual reading of the Agricultural Agreement supports the placement of the conservation, energy efficiency and renewable energy programs (with the two exceptions noted above) in the green box. Part III explains why the SCM Agreement, in all likelihood, does not make the conservation and renewable energy and energy efficiency payments vulnerable to serious challenge.

I. OVERVIEW OF WTO AGREEMENTS AND AUTHORITIES

The World Trade Organization ("WTO") oversees the dispute resolution process regarding the General Agreement on Tariffs and Trade ("GATT") and subsequent multilateral agreements entered into under WTO auspices. The basic purpose of the GATT/WTO regime is to compel member nations to make transparent and reduce non-tariff barriers to trade, but the GATT/WTO regime from its inception has also recognized that the regime needs to accommodate domestic policy concerns of its member states, including concerns regarding environmental protection and natural resource preservation. Article XX to the original GATT, for example, provides for an exception to the bar on trade restrictions for domestic measures necessary to protect plant, animal or human health. In addition, GATT/WTO agreements should be interpreted by the WTO decisionmakers to be consistent with other multilateral international agreements and principles of customary international law, including principles of customary international law relating to the environment. *See, e.g.*, Robert Howse, *Adjudicative Legitimacy and Theory Interpretation in International Trade Law*, in THE EC, THE WTO, AND THE NAFTA: TOWARDS A COMMON LAW OF INTERNATIONAL TRADE 54-56 (J.H.H. Weiler, ed. 2000).

In addition to the texts of GATT and WTO agreements, the principal sources of WTO law are decisions by WTO panels and by the WTO appellate body to which panel decisions can be referred. Although WTO appellate body decisions do not have the same precedential force as,

for example, United States Supreme Court opinions in the context of United States federal law, the appellate body decisions are treated as highly persuasive authority in WTO disputes.

Two agreements bear on the question of the legality of Title II and IX subsidies to farmers within the GATT/WTO regime. The first agreement is the Agreement on Subsidies and Countervailing Measures. This agreement is written in general terms: it does not address particular sectors such as agriculture. The SCM Agreement has a number of important features. First, Article 1.1(a) defines subsidy in broad, economic terms to include any financial contribution by a government that confers a benefit to an entity. Second, Article 2 limits many of the restrictions in the agreement to "specific" subsidies, those that are explicitly or de facto directed at specific enterprises, industries or groups. Third, Articles 5 and 6 make actionable specific subsidies that have the effect of causing "serious prejudice to the interests of another" WTO member, and prejudice is defined to include, inter alia, cases in which the subsidy results in "an increase in the world market share of the subsidizing Member in a particular subsidized primary product or commodity as compared to the average share it had during the previous three years and this increase follows a consistent trend over a period when subsidies have been granted." As a practical matter, complaint proceedings under the SCM Agreement often entail competing testimony by econometric experts regarding the market effects of various government measures.

The Agreement on Agriculture establishes particular rules for domestic supports of agriculture. The principal conceptual distinction in the Agreement is between "green box" supports and "amber box" supports. Green-box subsidies are exempt from any restrictions in number or aggregate dollar amount: a member state may have as many and as large green box supports as it wishes. By contrast, the Agreement on Agriculture, along with subsequent rounds of talks among the member nations, have established a schedule for the reduction in the aggregate level of amber box domestic support provided by each member to its farming industry. Thus, for the purposes of the Agricultural Agreement, a great deal turns on the classification of domestic supports as either green box or amber box.

II. STATUS OF U.S. PROGRAMS UNDER THE AGREEMENT ON AGRICULTURE

A. Textualism And The WTO

In approaching the question of whether U.S. conservation, energy efficiency, and renewable energy programs fall within the green box established by Annex 2 to the Agreement on Agriculture, the focus must be the text – the precise words – of the Annex. This is because the well-established interpretive methodology of WTO decisionmakers – and the Appellate Body in particular – is strictly textual. *See* John H. Knox, *The Judicial Resolution of Conflicts Between Trade and the Environment*, 28 HARV. ENVTL. L. REV. 1, 48 (2004) (explaining that "[w]here possible" the Appellate Body "has relied on the ordinary meaning of the language in the trade agreement before it)." As the Appellate Body has explained, "the basic principle of interpretation that the words of a treaty [must] be given their ordinary meaning" requires the WTO to "take adequate account of the words actually used in the treaty." Report of the

Appellate Body, *United States-Standards for Reformulated and Conventional Gasoline*, AB-1996-1, April 29, 1996, WETO Doc. Wt/DST/AB/R (hereafter "*Reformulated and Conventional Gasoline*"), at 11. In the view of the Appellate Body, "[a] treaty interpreter must begin with, and focus upon, the text of the particular provision to be interpreted. It is in the words constituting that provision, read in their context, that the object and purpose of the states parties to the treaty must first be sought." Report of the Appellate Body, United *States – Import Prohibition of Certain Shrimp and Shrimp Products*, AB-1998-4, Oct. 12, 1998, WTO Soc. WT/DS58/AB/R (hereafter "*Shrimp Products*"), at par. 14.

The textual focus of the WTO decisionmakers reflects a compelling need on the part of the WTO – the maintenance of legitimacy among a large politically and culturally diverse membership – and hence is unlikely to diminish or disappear. Textualism aids legitimacy by providing a relatively objective or verifiable basis for decisions that otherwise might be suspected of reflecting simply the political preferences of WTO decisionmakers. As John Knox makes the point, a "literalist" mode of interpretation is "an obvious route" for a tribunal seeking support for its decisions. Knox, *supra* at 49. Two influential former members of the WTO Appellate Body – James Bacchus and Claus-Dieter Ehlermann – have spoken quite openly about the legitimacy imperatives underlying WTO textualism. *See* Claus-Dieter Ehlermann, *Six Years on the Bench of the "World Trade Court": Some Personal Experiences as Member of the Appellate Body of the World Trade Organization*, 36 J. WORLD TRADE 605, 617 (2002) (explaining that "the method of literal interpretation is relatively safe" in that "its results are more easily accepted than results reached by other interpretive tools"); James Bacchus, *Table Talk: Around the Table of the Appellate Body of the World Trade Organization*, 35 VAND. J. TRANSNAT'L L. 1021, 1033 (2002) (indicating that the need for a verifiable rationale means that "the words of the treaty is thus our constant focus in reaching and rendering judgments").

B. The "Basic Criteria" Of Paragraph 1 Of Annex 2

Given the textual focus of the Appellate Body's interpretation of treaties, a central question is: what does the plain text of Annex 2 require for a government payment to farmers to qualify for green box status? In answering this question in the context of Title II and IX payments, only four paragraphs of Annex 2 are pertinent. Paragraph 1 sets forth "basic criteria" that all government supports must meet to qualify for the green box. Paragraph 5 provides that, with respect to government supports that take the form of "Direct payments to producers," the supports also must meet the requirements of paragraphs 6, 7, 8, 9, 10, 11, 12 or 13 in order to qualify for the green box. Paragraphs 6-9, 11, and 13 cannot be read as relevant to the United States conservation, energy efficiency or renewable energy programs. Paragraphs 10 and 12, as discussed below, can be read as pertinent to these programs. Paragraph 10 references "resource retirement programmes," and paragraph 12 references "Payments under environmental programmes." Thus, for the United States conservation, energy efficiency, and renewable energy payments to qualify for the green box, those payments must meet the basic criteria set out in paragraph 1 and the additional requirements set out in paragraph 10 or 12.

According to the first sentence of the first paragraph of Annex 2, green box government supports must "have no, or at most minimal, trade-distorting effects or effects on production."

The second sentence then states: "Accordingly, all measures for which [the green box] exemption is claimed shall conform to the following basic criteria: (a) the support in question shall be provided through a publicly-funded government programme . . . and, (b) the support in question shall not have the effect of providing price support to producers . . ." The word "Accordingly" in the paragraph has only one "ordinary" or "natural" meaning: that the no or minimal trade distortion requirement mandates, and is satisfied by, the two basic criteria of public funding and no price supports. Because the United States' conservation, energy efficiency and renewable energy programs are publicly funded and do not entail price supports, they meet the requirements of paragraph 1.

In the ongoing dispute over United States subsidies for upland cotton, however, Brazil has suggested that paragraph 1 requires an independent showing of no trade-distorting effects in addition to the satisfaction of the two basic criteria. The panel in the cotton dispute reportedly has issued an interim, confidential report which may or may not address Brazil's reading of paragraph one. Brazil made many arguments at the WTO in support of its claim that United States cotton subsidies are unlawful, see *United States - Subsidies on Upland Cotton, Request for Consultations by Brazil*, Oct. 3, 2003, WT/DS276/1, and the panel could have relied on one or more of many different legal theories. Even if the panel does accept Brazil's reading of paragraph 1, the Appellate Body might overturn the panel on the ground that Brazil's reading eliminates by fiat the word "Accordingly" from the second sentence of paragraph 1, which is decidedly a non-textualist approach. Brazil's reading may also be contrary to the WTO regime's – and the Appellate Body's – decided preference for relatively crystalline rules as opposed to muddy standards. As the United States has argued, "[a]ssessing the conformity of a claimed green box measure against the [no-trade-distorting requirement] of the first sentence in isolation would be a difficult task for a Member and for a panel. Therefore, Members agreed that if a measure 'conform[s] to the . . . basic criteria of the second sentence plus any applicable policy-specific criteria, it shall have been deemed to have met the . . . requirement of the first sentence of Annex 2.'" Rebuttal Submission of the United States, *United States – Subsidies on Upland Cotton*, Aug. 22, 2003, WT/DS 267, at par. 17.

C. The Additional Requirements Of Paragraphs 10 And 12

1. Paragraph 10 and the Conservation Reserve Program

The Conservation Reserve Program in Title II of the Farm Security Act is a land retirement program, which must meet the four requirements set forth in paragraph 10 of Annex 2. These requirements, in brief, are: (a) defined eligibility criteria; (b) removal of land from agricultural production for at least three years; (c) the government cannot mandate other uses of retired land; and (d) government payments cannot be related to the type or quantity of production of any land remaining in production. The Conservation Reserve Programs (including the Wetland Reserve Program) straightforwardly meet these requirements. 16 U.S.C. § 3831(b) and (h)(2), set forth specific eligibility criteria. The reservation period appears to be 10 or 15 years, which exceeds the three-year minimum. 16 U.S.C. § 3831(e). Finally, there is nothing in the statutory text that suggests that the United States dictates particular productive uses for retired land or ties retirement payments to continuing production on non-retired land.

2. Paragraph 12 and the Conservation Security Program and Environmental Quality Incentives Program in Title II of the Farm Security Act

In order to qualify as green box payment programs, the Conservation Security Program and environmental quality incentives in Title II must satisfy the two requirements of paragraph 12 of Annex 2. Those two requirements, which are also relevant to the status of the Title IX programs, as discussed below, are as follows:

> (a) Eligibility for such payments shall be determined as part of a clearly-defined environmental or conservation programme and be dependent on the fulfillment of specific conditions under the government programme, including conditions related to production methods or inputs.
>
> (b) The amount of payment shall be limited to the extra costs or loss of income involved in complying with the government programme.

Annex 2, par. 12.

The Conservation Security Program, which provides funding for farmers who engage in conservation practices on agricultural land, meets the first requirement of paragraph 12: the program plainly reflects an environmental purpose, and sets specific eligibility criteria that relate to production or inputs. *See* 16 U.S.C. § 3838 (c)(4) & (c)(5) (specifying conservation practices such as water quality management and invasive species management and providing that conservation security plans should address significant resources of concern at a level that "meets the appropriate nondegradation standard.")

What is less obvious is whether the Conservation Security Program in all cases meets the second requirement of paragraph 12. The statute provides that participating farmers shall receive between 5% and 15% of the rental value of the land covered by the conservation contract *and* between 75% and 90% of the actual costs of implementing the conservation practices specified in the contract. It is possible that in some cases the rental payment plus the actual costs payment would exceed 100% of the "extra costs . . . involved in complying with the government programme." In any such cases, green box status would be inapplicable. The Conservation Security Program is now only in the rulemaking stage, so characterizations of how it will operate are very difficult to make.

The analysis is much the same with respect to environmental quality incentives, which are payments to encourage land management or structural practices on private agricultural land that the Secretary of Agriculture "determines [are] needed to protect . . . water, soil, or other resources from degradation." 16 U.S.C. § 3839 aa-1 & aa-2. This program certainly satisfies requirement (a) of Paragraph 12, but it may, in some instances, fail to meet requirement (b). Farmers may receive up to 75% of the costs of implementing structural and/or land management practices plus "incentive payments in an amount and at a rate determined by the Secretary to be necessary" to encourage participation by producers. *Id.* In those cases in which the actual costs payment plus the incentive payment exceed 100% of the total costs of compliance, green box status would be inapplicable. The United States Department of Agriculture is just beginning to

implement the Conservation Security Program, so characterizations of how it will operate are very difficult to make.

3. Paragraph 12 and the Energy Efficiency and Renewable Energy Payments In Title IX of the Farm Security Act

Whereas the (b) requirement of paragraph 12 is the problematic issue with respect to the Title II conservation programs, it is the (a) requirement—and in particular the requirement that the payments be made pursuant to an environmental or conservation program—that is potentially problematic in the Title IX context. On balance, the Title IX programs are "environmental or conservation" programs within the WTO framework, and hence all the Title IX energy efficiency and renewable energy payments fall within the green box.

Section 9006 of the Farm Security Act directs the Secretary of Agriculture to make loans, loan guarantees, and/or payments to farmers to "purchase renewable energy systems" and "make energy efficient improvements." 7 U.S.C. § 8106(a)(1)-(2). Eligibility for payments is based on demonstrated financial need. 7 U.S.C. § 8106(b). The Secretary's grant or loan amounts must be based on consideration of, *inter alia*, expected energy savings and expected environmental benefits of renewable energy systems. 7 U.S.C. § 8106(c)(2). The Act thus seems to differentiate between "energy savings" and "environmental benefits," although energy savings are a kind of environmental benefit. For WTO purposes, it would be helpful for Congress in its farm legislation to expressly identify the objectives of energy efficiency and renewable energy programs as environmental objectives. The substantive truth is that the energy efficiency programs are a type of environmental programs that produces environmental benefits, and Congress' distinction between the "energy savings" and "environmental benefits" should thus be eliminated by Congress in subsequent legislation.

The key term implicated by the Section 9006 program is "environmental or conservation programme." The Agreement on Agriculture does not define that term. In the context of interpreting GATT Article XX exceptions to the bar against non-tariff trade restrictions, the Appellate Body has interpreted the term to mean a measure "primarily aimed" at conservation objectives. *Reformulated and Conventional Gasoline*, *supra* at 11. By the same logic, a program that is primarily aimed at conservation objectives presumably would constitute a conservation programme within the meaning of paragraph 12 of Annex 2. Thus, properly framed, the inquiry is whether a program that encourages energy efficiency and/or greater reliance on renewable energy is "primarily aimed" at environmental and conservation objectives.

It seems beyond dispute that, in the WTO framework, greater energy efficiency and reliance on renewables are cognizable environmental and conservation objectives. The Appellate Body has endorsed the goals of "the promotion of sustainable development" and "greater responsiveness of the multilateral trading system to environmental objectives set forth in Agenda 21, and the Rio Declaration . . . ." *Shrimp Products*, *supra* at par. 154 (quoting the Decision on Trade and Environment of the Ministers of Trade at the Marrakesh conference establishing the WTO). The WTO regime, in other words, recognizes and incorporates Agenda 21, which identifies greater energy efficiency and the environmentally sound use of renewable sources of energy as goals of sustainable development. *See* Agenda 21, Ch. 4, 4.17 &

4.18; *see also* Rio Declaration, Principle 8 ("To achieve sustainable development . . . States should reduce and eliminate unsustainable patterns of production . . .").

It also seems beyond dispute that the Section 9006 program is aimed at the twin goals of greater energy efficiency and greater use of renewables. Indeed, on its face, these are the only objectives of that program. The Section 9006 program thus should be understood as primarily aimed at environmental and conservation objectives and thus qualifies as an environmental and conservation program within the meaning of paragraph 12 of Annex 2.

A critic of the Section 9006 program might argue that its primary energy efficiency objective is actually to confer an economic benefit on farmers (in the form of reduced energy costs), and that the environmental and conservation benefits of the program are merely incidental. This argument, however, would seem to require the United States to prove something that is inherently improvable – namely, what motivated legislators more, helping farmers or helping the environment, in enacting a program in which the economic benefits to farmers and the environmental benefits are correlated. The WTO framework is not designed to hamstring domestic environmental legislation, see *Shrimp Products*, *supra* at par. 129 (confirming that the WTO regime recognized "the importance and legitimacy of environmental protection as a goal of national and international policy"), and that would be precisely the situation if the United States were required to "prove the improvable" as a condition of pursuing environmental objectives through green box subsidies. Moreover, in any trade dispute, it is the challenger who bears the burden of proof and persuasion.

Nonetheless, it does seem to me that, if the United States were confronted with a challenge to the green box status of the Section 9006 program, it would be helpful to be able to show that environmental benefits yielded by the program are indeed significant. Documented results do matter. *See Reformulated and Conventional Gasoline*, *supra* at 14 (explaining that "[i]n a particular case, should it become clear that realistically, a specific measure cannot in any possible situation have any possible effect on conservation goals, it would very probably be because that measure was not designed as a conservation regulation to begin with. In other words, it would not have been 'primarily aimed' at conservation . . .at all."). If the United States desires to "green box-proof" future energy efficiency and renewable energy programs, it may be sensible, at a minimum, to establish a requirement of periodic documentation by the Secretary of Agriculture of the environmental benefits realized by the federal payments and loans to enhance energy efficiency and invest in renewable energy systems. The United States already has in place a system for calculating expected environmental benefits as part of the loan or grant review process; this system would be helpful in the context of a WTO challenge, but only if there are safeguards or checks to verify that the anticipated environmental benefits actually accrue. The stronger the record of environmental benefits, the more assured that it will have green box status.

Finally, Section 9006 program meets the second "(b)" requirement of paragraph 12 of Annex 2 because the statute provides that federal loan and grants can cover at most 50% of the out-of-pocket costs of improving energy efficiency and renewable energy systems investments (which, in this context, is the cost of compliance with the government program within the meaning of paragraph 12(b)).

D. The Section 9010 Bioenergy Program

The Section 9010 Bioenergy Program of Title IX provides for payments to producers of "bioenergy" based on the number of gallons of bioenergy produced. Bioenergy is defined as biodiesel and fuel grade ethanol. 7 U.S.C. § 8108(a)(2). The bioenergy program is not a green box program: Annex 2 provides eight sets of requirements or descriptive criteria for "Direct payments to producers" (that is, the requirements/criteria set out in paragraphs 6, 7, 8, 9, 10, 11, 12, and 13), and the bioenergy program does not meet any of those sets of criteria. Nonetheless, as discussed below, some bioenergy payments are outside the purview of any WTO limitations on direct government payments to farmers.

There is no GATT/WTO problem with the Section 9010 program to the extent that the bioenergy is produced with animal wastes, grasses, crop "wastes" or other materials that are not grown and marketed as agricultural commodities by other WTO members. In such cases, the bioenergy program does *not* operate as a downstream production subsidy for an agricultural commodity because the upstream inputs—corn husks, grasses and the like—are not agricultural products that are the subject of international trade (or given the transportation costs, likely to ever be so). From the standpoint of concerns regarding agricultural subsidies, the subsidization of the production of bioenergy in the form of cellulosic ethanol is thus wholly permissible within the WTO framework.

If the United States-produced bioenergy ever captured significant market share in the United States energy market, the argument could be made that the Section 9010 program is an unlawful subsidy of domestic energy producers. This contingency would seem to be remote given the relatively immature state of bioenergy technology and the bioenergy industry in the United States, and, in any event, energy production worldwide is so suffused with heavy-handed government intervention and subsidization that it would be difficult for any country to make an argument that the United States is or would be operating outside what is, in effect, the norm. Significantly, there have been no SCM actions in the WTO relating to domestic supports for energy production.

Whether the Section 9010 program would be viewed by a WTO panel as an amber box, domestic production subsidy for corn or soybeans that can be used to produce bioenergy would depend on the existence or non-existence of a *de facto* requirement or at least understanding that eligible commodities would be United States-grown. Section 9010 defines an eligible commodity—a commodity eligible for use in producing bioenergy—in terms of the type of crop (e.g., corn, soybeans), and not the nation of origin of the commodity. It is thus possible that, for example, subsidized United States bioenergy producers could use Canadian corn as their feedstock. But if it is the reality of bioenergy production that it is always economical to use feedstocks that are locally grown (to reduce transportation costs for large, bulk purchases, and instead exploit excess, below-grade product in the immediate area), then the Section 9010 program could be understood as establishing a *de facto* production subsidy for eligible commodities grown in the United States.

E. Research and Development Programs Relating to Bioenergy and Biofuels

The 2002 Farm Bill includes some research and development provisions for bioenergy/biofuels, and future legislation may have an even greater R&D focus. Under Annex 2 of the Agreement on Agriculture, there are two ways for R&D programs to qualify for green box status. First, for R&D programs that do not involve direct payments to producers or processors, R&D is permitted, apparently without limit, even if the research is simply "general research" or research "relating to particular products." Annex 2, paragraph 2(a). Second, for government R&D programs that do involve direct payments to producers, those payments are permissible under paragraph 12 of Annex 2 if the payments are part of "a clearly defined environmental or conservation programme," and if the payments are limited to producers' extra out-of-pocket or loss-of-income costs of participating in the program. Thus, payments to producers that are part of R&D projects are most likely to survive a challenge to their status as green box subsidies if they can be shown to be part of a bona fide environmental program; that showing, in turn, will be strengthened by governmental documentation of the environmental rationale, the expected environmental benefits and the realized environmental benefits of the payments. It will also be important for the government to be able to document that producers did not realize net profits as a result of participation in R&D projects and receipt of government payments for that participation.

III. RECONCILING THE AGREEMENT ON AGRICULTURE AND THE SCM AGREEMENT

So far, this memorandum has addressed only the characterization of United States programs under the Agreement on Agriculture. This Part explores this question: Even if the United States conservation, energy efficiency and renewable energy programs do qualify for the green box, can the programs nonetheless be challenged successfully under the SCM Agreement as "specific subsidies" that seriously prejudice other WTO members by increasing "the world market share" of the United States in subsidized products? This is not an easy question but, on balance, the answer is "no."

It is important to underscore that the SCM Agreement requires a complaining WTO member to *prove* that a specific subsidy enhances the subsidizing country's market share in a particular subsidized product.[3] By contrast, reductions in amber box supports are required by the Agreement on Agriculture in the absence of any showing of a connection between particular amber box subsidies and world market shares in particular products. Thus, even if green box subsidies can be challenged under the SCM Agreement, there is real value in the green box status because it means that subsidies with that status are not subject to challenge automatically, but rather only upon showing that the subsidies alter world market shares.

[3] Proving a link between a subsidy and changes in market share is no easy task, in part, because the WTO does not accept mere correlation as definitive proof of causation. *See* Richard H. Steinberg & Timothy E. Josling, *When the Peace Ends: The Vulnerability of EC and US Agricultural Subsidies to WTO Legal Challenge*, 6 J. INT. EC. L. 369, 390-91 (2003) (exploring difficulties of establishing causation).

Article 13 of the Agreement on Agriculture explicitly precludes challenges to green box subsidies under the SCM Agreement before January 1, 2004. The Agreement does not state that green box subsidies are subject to challenge after January 1, 2004; rather the Agreement is simply silent on this subject.

The question of how green box subsidies should be treated after January 1, 2004 could be decided in one of two ways – by a new round of multilateral negotiations culminating in a new agreement regarding the status of green box subsidies, or, in the absence of such an agreement, in a legal decision by the WTO Appellate Body on the status of green box subsidies under the relevant existing agreements (the SCM Agreement and the Agreement on Agriculture). It is, of course, impossible to predict with any high degree of assurance what new rounds of multilateral negotiations will bring. It is clear that both the United States and the European members support a continuation of green box protection from challenge. For their part, most developing countries do not seem adverse to green box subsidies related to environmental programs per se, but they are unhappy that the green box does not encompass development programs. To the extent that developing countries are frustrated with the United States' agricultural practices, the focus is primarily export subsidies and tariff constraints on market access for developing countries' agricultural products. There do not seem to be the makings of a multilateral political consensus to eliminate protection for green box subsidies related to environmental programs.

If there is no resolution of this issue in new rounds of multilateral talks, then the WTO Appellate Body will likely be called upon to decide the issue based on the texts of two existing agreements: the SCM Agreement and the Agreement on Agriculture. One might argue that, by explicitly precluding challenges to green box subsidies up until January 1, 2004, the drafters of the Agreement on Agriculture implied that challenges after that date are permitted. But it is equally likely that the drafters did not want to take an explicit position on this issue, perhaps because they wished to encourage later negotiations among WTO members regarding the interplay of the SCM Agreement and the Agreement on Agriculture. In any event, because the WTO's interpretive mode is determinedly textual, the WTO Appellate Body is unlikely to be open to arguments based on speculations regarding the drafters' intent.

In the face of textual silence on the question of the treatment of green box subsidies under the SCM Agreement after January 1, 2004, how would the WTO Appellate Body decide this issue? One possibility is that the WTO decisionmakers would rely on two principles—what might be termed the specificity principle and the sustainable development principle. In the *EC-Bananas* case, the Appellate Body held that GATT and other multilateral agreements applied to agricultural products "except to the extent that the [Agricultural Agreement] contained specific provisions dealing specifically with the same subject matter." Report of the Appellate Body, *EC—Regime for the Importation, Sale, and Distribution of Bananas*, WT/DS 27/AB/7, Sept. 9, 1997, pars. 155-158. Following *EC-Bananas*, because the Agricultural Agreement is more specific regarding the permissibility of agricultural subsidies than the SCM Agreement, it should trump the SCM Agreement in the face of textual silence regarding the relationships between the two agreements. *See* Didier Chambovey, *How the Expiry of the Peace Clause (Article 13 of the WTO Agreement) Might Alter Disciplines on Agricultural Subsidies in the WTO Framework*, 36 J. WORLD TRADE 305, 305-52 (2002) (developing this argument).

Moreover, the Appellate Body interprets textual ambiguities in WTO agreements in light of "the specific language of the preamble to the [agreement establishing the WTO], which, we have said, gives color, texture and shading to the rights and obligations of Members . . .". *Shrimp Products*, *supra* at par. 155. As the Appellate Body in *Certain Shrimp Products* emphasized in broadly construing the term "exhaustible natural resources" under Article XX of GATT, the WTO preamble calls for "the optimal use of the world's resources in accordance with the objective of sustainable development, seeking both to protect and preserve the environment and to enhance the means for doing so . . .". *Id.* at par. 129. Thus, the objective of sustainable development gives "color" or "shading" to WTO resolutions of textual ambiguity. It would seem to follow that the Appellate Body would construe the Agricultural Agreement as precluding post-January 1, 2004 challenges under the SCM Agreement to green box subsidies that plainly advance the objective of sustainable development, which the United States conservation, energy efficiency and renewable energy programs do.

Of course, it is possible that the Appellate Body would wish to preserve some special protection from SCM challenges for green box subsidies that promote sustainable development, but not protect such subsidies from SCM challenges altogether. However, it would be difficult for the Appellate Body to articulate a compromise rule of this sort with respect to green box subsidies that would be certain and coherent enough to give meaningful guidance to WTO members. Since the Appellate Body presumably would wish to avoid sowing confusion among its members, it would likely gravitate toward a crystalline rule—i.e., either that green box challenges that promote sustainable development are subject to challenge under the SCM Agreement, or that they are not. WTO decisionmakers are more likely to adopt the latter rule because, as discussed above, the latter rule better conforms to interpretive principles of the primacy of specificity and the advancement of the objective of sustainable development.



ENVIRONMENTAL LAW & POLICY CENTER

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