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In Absence Of Cotton Payments, Brazil Moves Closer To Trade Retaliation

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Senior Brazilian government officials this week are expected to decide to impose hundreds of millions of dollars in trade retaliation against U.S. exports, as another month closes without any signal that the U.S. will pay the monthly $12.25 million it agreed to pay Brazil as part of an interim settlement to a long-standing fight over farm subsidies.

According to sources familiar with the Brazilian government's deliberations, a special inter-ministerial group known as CAMEX is slated to convene on Nov. 27 and consider a "menu" of options in terms of the monetary value, method and timing of imposing trade retaliation, as well as which sectors will be affected.

One key aspect of that debate is whether Brazil should suspend U.S. intellectual property rights (IPR) protections as part of its retaliatory measures, or if it should only impose retaliatory tariffs on goods.

While the Brazilian government has thus far been cautious, these sources said Brasilia now feels it has been backed into a corner and has no choice but to finally retaliate. The U.S. administration has cut the regular settlement payment since October and thus is clearly in breach of its end of the deal, without any move to bring itself into compliance with the World Trade Organization ruling at the root of the fight, sources noted.

Under the interim settlement, reached in 2010, the U.S. agreed to pay the Brazil Cotton Institute -- a special organization devoted to bolstering Brazilian cotton production -- a total of $147 million annually. In return, Brazil suspended the retaliation it was authorized to impose by the WTO after it successfully proved that U.S. farm subsidies, including those for cotton producers, were WTO-illegal.

The settlement was supposed to be in place only until the U.S. brought itself into compliance through the next U.S. farm bill. But passage of new legislation has faced a multitude of challenges for the past two years, and a House-Senate conference is now continuing to struggle to pass a bill before the end of 2013.

U.S. and Brazilian business groups have been making a last-ditch effort to try and convince the White House to restart the payment in order to head off Brazilian retaliation. But as of this morning (Nov. 25), they were doubtful that Washington would chance its stance, according to one business source.

In August, U.S. Agriculture Secretary Tom Vilsack said his department would no longer make the cotton payments to Brazil, citing a lack of authority. Policy experts, however, have said this is tactical and that the department does in fact have that discretion (*Inside U.S. Trade*, Aug. 16).
In a report released earlier this month arguing for the importance of passing the farm bill, the White House noted that the administration had suspended the payments, saying it was "in part due to sequestration." It also urged Congress to act quickly in order to avoid retaliation, saying that "Congressional action on a Farm Bill is absolutely necessary to reach a full and final agreement with Brazil."

Business sources last week said the administration's decision not to make the payments anymore seemed to be aimed at setting up a scenario where it can blame Congress if retaliatory measures come into effect, and worried that the issue has been subsumed into the larger political fight between Republican lawmakers and the White House.

The Brazilian deliberations on whether to revoke IPR protections as part of its retaliatory measures hingeson whether to use the relevant trade data from the time the settlement was reached, in 2010, or more current data. The data influence the overall amount of retaliation Brazil is entitled to, and beyond a certain threshold, Brazil is authorized to suspend IPR protections as a form of so-called "cross retaliation."

Declining bilateral trade flows since 2010 -- due in part to China becoming Brazil's leading trading partner -- and purposeful tweaking to a U.S. agricultural export credit program also faulted in the case have diminished Brazil's retaliation rights downward to about $500 million. This is below the threshold beyond which it would be able to suspend IPR in cross-retaliation (*Inside U.S. Trade*, June 22, 2012).

By way of comparison, that is about half of what Brazil would be entitled to using data from 2008 or 2009, which gave it rights to $829 million and $1 billion in retaliation, respectively. Brazil enjoyed about $269 million in cross retaliation rights if 2008 data is used, and about $550 million if 2009 data is used.

Brazilian officials have held open that -- because the interim settlement with the U.S. was brokered in 2010 -- they may be able to impose the $1 billion in retaliation it was entitled to at that time, because its rights were effectively frozen by the deal. However, U.S. officials would likely dispute that approach, sources have said.

Another factor that Brazilian officials will be looking at is who exactly should be affected by the retaliation measures -- in goods and, possibly, in IPR. Last month, CAMEX directed a technical body to draw up by Nov. 30 a list of products imported from the U.S. against which Brazil could impose trade retaliation (*Inside U.S. Trade*, Oct. 11).

In 2010, Brazil released a final list of goods against which it was set to impose trade retaliation, targeting wheat, automobiles and cotton products. It also preliminary proposed a number of steps to rescind intellectual property protections -- including, for example, reducing the patent protection term for rights over medicine for a limited time.

But changing trade flows may have also made those goods less relevant, and so CAMEX will likely make any decisions based on the updated list, one business source said. It was not clear whether the technical group had also been drafting a new list of possible IPR measures that could be imposed.

The threat of Brazilian trade retaliation looms even as efforts the next U.S. farm bill struggle to advance inthe U.S. Congress. The leaders of the two congressional agriculture committees are slated to hold a conference call tonight (Nov. 25) to try and hash out some of the remaining issues, but there are significant hurdles still in the way, House Agriculture Committee Ranking Member Collin Peterson (D-MN) told a radio program last week.

Rep. Frank Lucas (R-OK), chairman of the House Agriculture Committee, in a separate radio interview with *The Oklahoma Farm Report* laid out three areas where there are significant gaps between the conferees: the nutrition title, the dairy program and supply management, and the structure of the commodity title.

On the latter issue, Lucas said the fight centers over whether new commodity safety net programs should pay farmers for income losses relative to a historical benchmark for crop plantings, also known as "base" acres, or on the actual crop they have put in the ground, known as "planted" acres.

The chairman said using base acres can be problematic politically because payments can be doled out to individuals who may not be farming. But he acknowledged that subsidies linked to planted acres are considered to be trade-distorting, "amber box" subsidies by the WTO. The U.S. faces a cap of $19.2 billion in annual amber box payments.

Another third option that is being considered allowing farmers to receive payments on planted acres, but only if they do not surpass a historical base, according to Lucas. "So that's just an example of one of the many nuances that we're trying to work through," he said.

The chairman expressed confidence that once the commodity title issues are addressed, the other pieces of the debate can be hashed out more quickly. He said that an extension of the farm bill is unlikely due to opposition from Peterson and Senate Agriculture Committee Chairwoman Debbie Stabenow (D-MI) toward that option.

As far as timing for passage of a bill, however, Lucas said it was uncertain whether a bill could move through both chambers before the Christmas holiday recess. But although that would technically trigger the implementation of so-called "permanent law" -- farm subsidy legislation dating back to 1949 -- Lucas said it would likely be several weeks or a month for the U.S. Department of Agriculture to actually roll out those measures, giving lawmakers more time.