Bittersweet ‘subsidies’? Brazil files a WTO dispute against Thailand’s sugar regime

On 4 April 2016, Brazil filed a request for WTO consultations with Thailand regarding an alleged ‘subsidies’ scheme applicable to the sugar sector. It appears unlikely that the dispute will be resolved during the consultation period and while a final decision at the WTO is likely years away, this controversy, between the world’s two largest sugar exporters, looks poised to shake up the global sugar market in the near future.

This dispute has been expected for quite some time. The Thai sugar regime has already been the subject of discussions in multiple WTO fora during the last several years. In particular and most recently, Australia and the EU raised questions regarding the Thai sugar regime during a meeting of the WTO Committee on Agriculture on 4 June 2015, as did Brazil and the European Union (hereinafter, EU) during the Committee’s prior meeting on 4 March 2015. While Brazil’s questions remained unanswered during the course of 2015, Thailand responded to the EU’s questions on sugar prices and the involved entities. The issue was then the subject of discussions on the side-lines of the Tenth WTO Ministerial Conference in December 2015. Media reports in early March 2016 detailed Brazil’s efforts in preparation of filing the case. Representatives of Brazil’s Foreign Ministry noted at that time that the Thai sugar regime was complex and not just a simple case of export subsidies. Brazil is now alleging a violation of a large number of provisions of the WTO Agreement on Agriculture (hereinafter, AoA) and the WTO Agreement on Subsidies and Countervailing Measures (hereinafter, ASCM). Specifically, Brazil considers that Thailand violated Articles 3.2, 3.3, 6.3, 8, 9.1 and 10.1 of the AoA, as well as Articles 3.1(a), 3.2, 5(c) and 6.3 of the ASCM. Brazil alleges that Thailand is strictly controlling its entire sugar sector, including, e.g., the production, storage, transport, sale, import, export, and other activities applicable to cane, raw sugar, white sugar, molasses, and sugar by-products.

In its request for consultations, Brazil provided details of its interpretation of the Thai sugar quota and subsidies system. Firstly, Brazil specifically refers to the Thai quota system and the application of price controls. According to Brazil, Thailand has put in place a quota system that limits the quantity of sugar sold in Thailand and imposes price controls on ex-factory, wholesale, and retail sales of cane and sugar in Thailand. Allegedly, Thailand guarantees a certain price for sugar produced for domestic consumption. In addition, the system requires that sugar produced in addition to the quota be exported and not be sold on the domestic market. According to Brazil, the guaranteed prices are accompanied by supplemental payments to Thai sugar cane growers. Brazil asserts that this system is not
consistent with Thailand’s WTO obligations. WTO Members’ commitments are listed in so-called ‘Schedules of Concessions’. In the case of sugar, as with all agricultural products, these concessions and commitments relate to tariff rate quotas, limits on export subsidies and further kinds of domestic support. Brazil now asserts that Thailand has not listed any export subsidies in Section II of Part IV of its Schedule, which applies to specific commitments on domestic support and export subsidies on agricultural products. Therefore, Brazil alleges a violation of the AoA, more specifically of Articles 3.3 and 9.1 thereof. Secondly, apart from the sugar price regime itself, Brazil asserts that Thailand illegally subsidises the conversion of rice paddies to sugar cane production as a means to increase the capacity of sugar production from sugar cane. Adding this to the aforementioned sugar regime, Brazil asserts that Thailand exceeds the 10% de minimis level of support allowed for developing countries and thereby violates Articles 3.2 and 6.3 of the AoA. Finally, Brazil claims that Thailand also violated the ASCM through the implementation of its sugar regime. Specifically, Brazil mentions alleged violations of Articles 3.1(a), 6.3 as well as 5(c) and 6.3 of the ASCM.

While it likely expected this case to be filed, Thailand appears to be on the defensive. Reports indicate that the Deputy Secretary-General of the Cane and Sugar Industry Policy Bureau of the Ministry of Industry stated that the alleged payments do not qualify as a subsidy because they are not paid by the government, but instead come from the Thai Cane and Sugar Fund (hereinafter, CSF). This is the same argumentation as put forward in the answers to the EU’s questions within the WTO Committee on Agriculture. The CSF allegedly raises its money independently. However, the Government of Thailand confirms that, if the fund cannot raise enough money to realise the desired payments, the fund receives loans from the state-owned Bank for Agriculture and Agricultural Cooperatives (BBAC). Notably, a 2015 Report on the Thai sugar industry published by the US Department of Agriculture refers to the aforementioned Cane and Sugar Fund as ‘state run’. That same report suggests that Thai sugar production, as well as sugar exports, are continuing an upwards trend. This year alone, sugar exports are expected to increase significantly, likely by around 7-10%. This is particularly due to exports to other ASEAN Member States after duty free market access as part of the ASEAN Economic Community (AEC) that became effective on 31 December 2015. Production increases are largely attributed to Thailand’s five year Agricultural Restructuring Program spanning from 2015 to 2020, which does in fact provide incentives to transform rice paddies into acreage for sugar cane crops. However, adverse weather conditions and especially a severe drought have led to a temporary decrease in production during the 2015/2016 timeframe. Despite this temporary decrease in production, exports are still expected to continue growing. This is attributed to the expectation that exporters will empty out their inventories during the current time of higher world sugar market prices as droughts are continuing to affect other sugar producing countries as well. A core issue of the dispute may thus lie in the question of government control and/or influence as regards the Thai CSF, as well as the Bank for Agriculture and Agricultural Cooperatives.

Large scale implications for Thailand and the Thai sugar market are potentially looming ahead. Considering current tight supplies on the world sugar market, such implications are also likely to affect the global sugar market and sugar prices. The sugar policies of Thailand and India, both being important sugar producers and exporters, are blamed for costing Brazilian sugar producers up to 1.2 billion dollars a year in lost revenues. Brazil claims that the Thai sugar regime has severely impacted the sugar market and led to a significant decrease in global sugar prices. The respective market positions of Brazil and Thailand do appear to have changed during the last several years. Brazil’s global sugar market share decreased from 50% to 44.7% since 2012 while, during the same timeframe, Thailand’s market share increased from 12.1% to 15.8%. This leads to the likely assumption that, if the Thai sugar regime were to be found to violate WTO rules, the global sugar prices and market shares would be affected and global sugar prices could increase. However, this dispute is unlikely to see any short term resolution. WTO rules provide for a multi-tiered process and by
requesting consultations, Brazil only initiated the first step. The consultations, to be initiated within 30 days of the request, are intended to give the parties an opportunity to discuss the matter and to find a satisfactory solution without proceeding with litigation. Article 4(7) of the WTO Understanding on Rules and Procedures Governing the Settlement of Disputes provides that, if consultations have failed to resolve the dispute after 60 days, the complainant may request adjudication by a panel. This may then be followed by an appeal to the WTO Appellate Body and potentially by compliance proceedings in case of alleged non-compliance.

The dispute is already gaining large-scale attention and will likely attract the participation by several WTO Members. On 19 April 2016, the EU requested to join the consultations. For the reasons spelled out above, all interested parties (countries and business constituencies alike) should closely monitor these proceedings. Tight supply on the world sugar market and the end of the EU sugar quotas in October 2017 look poised to further influence sugar market dynamics. While regulators around the world appear to be choosing different approaches, they must remain within the limits of WTO trade rules. This WTO dispute, if fully played out, may set new interpretative boundaries in terms of what countries can do to support sugar production and to regulate sugar markets.

The new EU ‘conflict minerals’ regulation is taking shape

On 20 May 2015, the EU Parliament took action with respect to the EU Commission’s March 2014 proposal for a Regulation of the European Parliament and of the Council setting up an EU framework for supply chain due diligence through the self-certification of responsible importers of tin, tantalum, tungsten and gold originating in conflict-affected and high-risk areas (hereinafter, the Proposed Conflict Minerals Regulation). In particular, the EU Parliament adopted a large number of amendments to the voluntary mechanism proposed by the EU Commission, and voted in favour of a mandatory monitoring system for minerals originating from conflict-affected and high-risk areas. In addition, the Council of the EU, which originally supported the voluntary mechanism as suggested by the EU Commission, agreed, at the end of December 2015, on a position during the Luxembourg Presidency. However, a final resolution may not be achieved until the Slovakian Presidency in the second half of 2016, mainly due to divergences between de EU Parliament and the Council, but also due to the complexity of the issue.

The EU Commission proposed the Conflict Minerals Regulation in order to reduce the financing of armed groups by means of natural mineral resources in conflict-affected or high-risk areas. The proposal builds on existing internationally accepted due diligence principles and refers to the ‘OECD Due Diligence Guidance for Responsible Supply Chains on Minerals from Conflict-Affected and High-Risk Areas’ (hereinafter, the OECD Guidance). This reference reaffirms the EU’s commitment to support the rules within the framework of the OECD guidelines, adopted in 2011. Furthermore, the EU Commission’s proposal makes reference to Section 1502 of the United States ‘Dodd-Frank Wall Street Reform and Costumer Protection Act’ (hereinafter, the Dodd-Frank Act). The Dodd-Frank Act has a strong focus on the Democratic Republic of Congo and nine neighbouring countries. In general, for other areas in Africa, Asia and Latin America, there are only a few other regulations available. It is in this light that the EU sought to develop a regulatory framework that would contribute to improved transparency in the supply chains of natural mineral resources. Conflict minerals are defined as the minerals that support, economically, armed groups. The EU, OECD and US have committed to implement legislation, as well as guidance to companies, in order to eradicate human rights violations and avoid contributing to armed conflicts.
The Dodd-Frank Act was passed by the US Congress in 2010. Section 1502(b) of the Dodd-Frank Act requires companies to disclose annually the use of (potential conflict) minerals on a mandatory basis, and to declare whether those minerals originate from the Democratic Republic of Congo or an adjoining country. Section 1502 of the Dodd-Frank Act only applies to publicly traded companies listed on the US stock exchange (upstream and downstream). These companies are required to file periodic reports with the US Security and Exchange Commission (hereinafter, SEC) making annual disclosure regarding whether they manufacture products that incorporate conflict minerals (conflict minerals are defined by the Dodd-Frank Act as gold, tin, tungsten and tantalum coming from the Democratic Republic of Congo and its adjoining countries). However, the implementation process was not easy. Studies, by private parties and the SEC, concluded that the estimated implementation costs for the industry and for the companies were substantially high. In addition, the majority of these costs were borne by suppliers not directly subject to the SEC jurisdiction. Another experience during the Dodd-Frank Act implementation was the lack of clarification from the outset on whether companies should additionally report products containing non-metal derivatives of conflict minerals. The experience of implementing the Dodd-Frank Act demonstrates that the final draft of the EU Conflict Minerals Regulation should take these experiences into account in order to avoid creating unnecessary burdens to companies and to further avoid unnecessary costs without hampering the transparency on the origin of minerals.

The Proposed Conflict Minerals Regulation provides for a voluntary ‘self-certification as a responsible importer’ constructed on the basis of the OECD due diligence requirements. Such proposal would put in place a system whereby importers voluntarily obtain a certificate relating to the importation of the aforementioned minerals, regardless of the origin of those goods. In this regard, the EU Commission intended to set up a system in which control mechanisms and transparency rules are implemented in the supply chain of these minerals, from the point of origin up until the smelters and refineries that process them. The proposal also introduces a supply chain risk assessment and identification procedure based on the OECD model on supply chains in order to develop a global draft regulation and implementation process for identifying risks and developing strategies to prevent or mitigate adverse impacts. The draft regulation also proposes to introduce an audit mechanism. The audits would then be carried out by independent third-party auditors. These third-party auditors would evaluate the due diligence requirements of the supply chain and would set up a wide-reaching system of public reporting that would include, for instance, supply chain due diligence policies and practices for responsible sourcing online.

The divergence between the positions of the Council of the EU and the EU Parliament have led to the initiation of a trilogue process (informal tripartite meetings bringing together representatives of the EU Parliament, the Council of the EU and the EU Commission) focussing on several issues. In particular, discussions revolve around: 1) whether the system should be either voluntary or mandatory; and 2) whether the possibility to widen the scope of the regulation would affect companies’ operations. There are various challenges concerning the tracing of the minerals to the smelters or refiners. One challenge is the complexity of supply chains themselves. Another challenge lies in the limited capacity (or willingness) of suppliers and other supply chain actors to share and disclose information up and down the chain. A third important issue regarding traceability is how the proposal will deal with entities in non-OECD countries that do not wish to cooperate. The importance of a clear definition of what constitutes a ‘conflict-affected’ and ‘high-risk area’ also cannot be underestimated. Special attention should equally be given to the development of a support programme for micro and small-to-medium sized enterprises (MSMEs). In this regard, it is important to point out, that the EU Parliament included in its amendments a call for technical assistance and financial aid by the Commission’s COSME programme for MSMEs established in the EU. Finally, it is essential to adopt a regulatory framework that is practicable and that will not conflict with other regulations.
Currently, the Proposed Conflict Minerals Regulation is following the EU ordinary legislative procedure and is being discussed in the trilogue between the Council of the EU, the EU Commission and the EU Parliament. The final draft of the regulation looks poised to be adopted by the end of this year. Making the regulation applicable both inside and outside the internal market will be crucial to avoid harmful consequences for the EU internal market, because the regulation is estimated to apply to close to one million companies inside the EU or with interests within the EU. The main elements of discussion that will be relevant to assess the impact of the regulation are: 1) its mandatory or voluntary nature; 2) its geographic scope; 3) the obligations for EU importers to remain consistent with the 5-step framework of the OECD rules; 4) the EU recognition of supply chain due diligence schemes; 5) the ex-post checks by EU Member States’ competent authorities; and 6) the EU list of global responsible smelters/refiners. Interested parties must monitor the further discussions of the trilogue and should make their voices heard before the EU’s new Conflict Minerals Regulation becomes a reality by the end of 2016.

Are EU nutrient profiles still needed after the Dextro Energy judgment of the EU General Court?

On 12 April 2016, Members of the EU Parliament (hereinafter, MEPs) voted in favour of (with 402 votes for and 285 against, with 22 abstentions) a resolution on the Regulatory Fitness and Performance Programme (REFIT), which aims at consolidating better law-making procedures, simplifying EU law and reducing administrative and regulatory burdens. Point 47 of the resolution concerns nutrient profiles and calls on the EU Commission, “in view of the serious and persistent problems which arise in the implementation of Regulation (EC) No. 1924/2006 on nutrition and health claims made on foods [hereinafter NHCR], including problems of distortion of competition, to review the scientific basis of this regulation and how useful and realistic it is and, if appropriate, to eliminate the concept of nutrient profiles” and considers that “the aims of Regulation (EC) No. 1924/2006, such as ensuring that information which is provided concerning foods is true and that specific indications are given concerning fat, sugar and salt content, have now been achieved by Regulation (EU) No, 1169/2011 on the provision of food information to consumers”. The idea of not needing nutrient profiles under the NHCR can also be observed in a recent judgment of 16 March 2016 in Case T-100/15, Dextro Energy GmbH & Co. KG v EU Commission, where the EU General Court held that energy tablets, or ‘cubes’, consisting almost entirely of glucose, cannot bear health claims relating to the contribution to energy-yielding metabolism because, although scientifically true, such claims would encourage excessive consumption of sugars, which is not recommended under generally accepted nutrition and health principles.

In simple terms, the so-called nutrient profiles are generally intended to determine whether foods are, based on their nutrient composition, eligible to bear claims (see Trade Perspectives, Issue No. 13 of 26 June 2015). Nutrient profiles must ensure that foods high in, e.g., sugar, fat or salt, do not carry a nutrition or health claim (e.g., a lollipop that is claimed to be ‘low in fat’, breakfast cereals with very high sugar content claiming to be ‘high in vitamin D’). The application of nutrient profiles as an additional criterion in the NHCR aims at avoiding a situation where nutrition or health claims mask the overall nutritional status of a food product, which could mislead consumers when trying to make healthy choices in the context of a balanced diet. Article 4 of the NHCR foresees the setting of such nutrient profiles by the EU Commission. Said measure, designed to amend non-essential elements of the NHCR by supplementing it, must be adopted in accordance with the regulatory procedure with scrutiny. The development of nutrient profiles, originally scheduled for January 2009, has not been finalised. The EU Commission’s services have been working on an implementing measure on nutrient profiles based on an opinion of the European Food Safety Authority (hereinafter, EFSA) and taking into account criteria included in the NHCR and
consultations with interested stakeholders and EU Member States. When the first draft proposals for a system were presented for discussion in 2008 and 2009, EU Member States’ experts, the EU Parliament, and some quarters of the EU Commission, expressed serious concerns. A primary criticism was the draft proposal’s restrictive approach (e.g., very strict thresholds), which some believed would dissuade innovation and jeopardise the sustainability and development of a range of food categories in Europe. Moreover, some said that the system proposed could ultimately be used as a reference by regulators to apply restrictions on what are determined to be ‘bad foods’ in a number of other areas, such as advertising and taxation.

The Communication from the EU Commission to the EU Parliament, the Council, the European Economic and Social Committee, and the Committee of the Regions on the Work Programme 2016 (“No time for business as usual”) of 27 October 2015, announces an assessment of whether the current requirements for nutrient profiles are fit-for-purpose. This initiative has been strengthened by the REFIT resolution adopted by the EU Parliament. The EU Parliament’s resolution is not legally binding because it is an own initiative procedure and the EU Commission is still required to take a position, but it sends out a very strong political message.

Others argue that there is misuse of nutrition and health claims on food, and that nutrition profiles under the NHCR should be established. An April 2016 survey published by FoodWatch, a German NGO, evaluated 644 products in Germany and the Netherlands containing front-of-pack vitamin-related health claims. The survey found that 80% of the products were high in sugar, salt or fat. The products with the respective claims were evaluated according to the nutrient profile model established by the World Health Organisation (WHO). In February 2015, the WHO’s Regional Office for Europe presented its nutrient profiling tool to restrict the marketing of ‘HFSS foods’ (i.e., foods high in fat, salt or sugar) to children. The nutrient profile model is intended to help national authorities identify such HFSS foods and restrict their marketing to children.

In FoodWatch’s survey, very few of the claims made were based on naturally present nutrients in the products/foods, which revealed the alarming scale of how manufacturers add vitamins to HFSS foods in order to market them as ‘healthy’, done for commercial interests rather than for public health purposes. But FoodWatch also criticised the EU Commission for allowing this practice to take place by failing to set nutrient profiles to determine which products can make such claims, leaving the doors open for companies to add a few vitamins to sweets or sugary drinks in order to confer them a healthy image.

In the context of the overall nutritional properties of a product bearing a claim, the recent judgment of the General Court of the EU of 16 March 2016 in Case T-100/15, Dextro Energy GmbH & Co. KG v EU Commission (hereinafter, Dextro Energy) is of interest. There, Dextro Energy sought the annulment of an EU Commission Regulation that rejected certain health claims. Dextro Energy, a well-known producer of products such as energy tablets, or ‘cubes’, consisting almost entirely of glucose, desired to market its products’ performance-boosting qualities and applied for a number of related health claims under the NHCR. After being provided by Dextro Energy with relevant scientific studies, EFSA in its scientific opinions concluded that a cause and effect relationship exists between the consumption of glucose and contribution to energy-yielding metabolism. Nonetheless, the EU Commission adopted Regulation (EU) 2015/8 of 6 January 2015 refusing to authorise certain health claims made on foods, other than those referring to the reduction of disease risk and to children’s development and health (hereinafter, Regulation (EU) 2015/8), in which it turned down Dextro Energy’s glucose claims.

In Recital 14 of Regulation (EU) 2015/8, the EU Commission argued that, pursuant to Articles 6(1) and 13(1) of the NHCR, health claims need to be based on generally accepted
scientific evidence. Authorisation may also legitimately be withheld if health claims do not comply with other general and specific requirements of the NHCR, even in the case of a favourable scientific assessment by the EFSA. Health claims inconsistent with generally accepted nutrition and health principles should not be made. Although a cause and effect relationship has been established between the consumption of glucose and the contribution to energy-yielding metabolism, the use of such a health claim would convey a conflicting and confusing message to consumers, because it would encourage consumption of sugars for which, on the basis of generally accepted scientific advice, national and international authorities inform the consumer that their intake should be reduced. Therefore, the EU Commission concluded that such a health claim does not comply with Article 3(a) of the NHCR, which foresees that the use of claims should not be ambiguous or misleading. Furthermore, even if the concerned health claim was to be authorised only under specific conditions of use and/or accompanied by additional statements or warnings, it would not be sufficient to alleviate the confusion of the consumer and, consequently, the claim should not be authorised.

In *Dextro Energy*, the EU General Court held that it cannot be successfully disputed that the generally accepted nutrition and health principles taken into account by the EU Commission constitute a factor that is legitimate and relevant to the decision on the question of admission of the health claims at issue. In the light of those principles, a high level of protection must be guaranteed to the consumer. Moreover, the EU legislator has explicitly recognised the relevance of generally accepted nutrition and health principles for the consideration of the question of the approval of a health claim in recital 18 of the NHCR, according to which a health claim should not be made if it is contrary to these principles, if it encourages or condones excessive consumption of any food, or if it disparages good dietary practice.

In addition, the General Court applied the generally accepted nutrition and health principle not to consume too much sugar. Although there is a cause and effect relationship between the consumption of glucose and contribution to energy-yielding metabolism, Dextro Energy’s products’ ‘nutrient profile’ (i.e., of a product consisting almost exclusively of glucose) did not permit the respective health claim. Arguably, the ruling in *Dextro Energy* can be interpreted as establishing that generally accepted nutrition and health principles must be taken into consideration by EU Member States’ enforcement authorities in assessing claims on certain products, without a need for the establishment of nutrient profiles under the NHCR.

A similar reasoning could be applied to certain products like potato crisps and biscuits bearing palm oil-free claims. Palm oil-free claims made in a nutritional context are arguably not approved nutrition claims under the NHCR (see *Trade Perspectives*, Issue No. 4 of 20 February 2015). Producers of products bearing such claim often argue that whatever fat (other than palm oil) is used in a given product is nutritionally advantageous. Looking in detail at which products bear such palm oil-free claims, it is often potato crisps and biscuits. It could be argued that, in any event, products like potato crisps and biscuits, which are often HFSS foods, should not bear nutrition claims because they are often excessive in sugar and fat (be it butter, palm oil or other vegetable fats). In the words of the NHCR, its excessive consumption disparages good dietary practice.

It is important to remember that there are no unhealthy foods, only unhealthy diets with the consumption of too much HFSS food. There appears to be a serious problem with certain claims like added vitamins, glucose or palm oil-free on certain products like breakfast cereals, potato crisps and biscuits. The establishment of nutrient profiles under the NHCR aims at not permitting nutrition and health claims on HFSS foods. After the *Dextro Energy* judgment of the EU General Court, enforcement authorities in the EU Member States should arguably step in when claims that are contrary to generally accepted health and nutrition principles are made on specific products that are high in fat, sugar and/or salt. Developments in the EU on nutrient profiles should be closely monitored and operators should be prepared
to participate in shaping potentially upcoming EU legislation by interacting with EU Institutions, third country Governments, relevant trade associations and affected stakeholders.

Recently Adopted EU Legislation

Customs Law


- Commission Implementing Decision (EU) 2016/578 of 11 April 2016 establishing the Work Programme relating to the development and deployment of the electronic systems provided for in the Union Customs Code

Food and Agricultural Law


Other


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